APPENDIX A

UNITED STATES COURT OF APPEALS
NINTH CIRCUIT

Nos. 94-16041, 94-16142,
94-16143 and 94-16327

WILLIAM S. RICHARDSON; HENRY H. PETERS, JR.; OSWALD K. STENDER, MYRON B. THOMPSON, and MATSUO TAKABUKI, in their capacities as Trustees of the KAMEHAMEHA SCHOOLS/BERNICE PAUAHI BISHOP ESTATE,
Plaintiffs-Appellants,

V.

CITY AND COUNTY OF HONOLULU,
a Hawaii Municipal Corporation,
Defendant-Appellee,

and

HALE COALITION,
Intervenor.

WILLIAM S. RICHARDSON; HENRY H. PETERS, JR.; OSWALD K. STENDER, MYRON B. THOMPSON, and MATSUO TAKABUKI, in their capacities as Trustees of the KAMEHAMEHA SCHOOLS/BERNICE PAUAHI BISHOP ESTATE,
Plaintiffs-Appellees,

and

HALE COALITION,
Intervenor,

CITY AND COUNTY OF HONOLULU,
a Hawaii Municipal Corporation,
Defendant-Appellant.

WILLIAM S. RICHARDSON; HENRY H. PETERS, JR.; OSWALD K. STENDER, MYRON B. THOMPSON, and MATSUO TAKABUKI, in their capacities as Trustees of the KAMEHAMEHA SCHOOLS/BERNICE PAUAHI BISHOP ESTATE,
Plaintiffs-Appellees,

V.

HAWAII LEASEHOLDERS EQUITY COALITION,
Intervenor-Appellant,

and

CITY AND COUNTY OF HONOLULU
a Hawaii Municipal Corporation,
Defendant.

SMALL LANDOWNERS OF OAHU,
Plaintiff-Appellant,

V.

CITY AND COUNTY OF HONOLULU'
Defendant-Appellee.

Argued and Submitted Nov. 2, 1995
Decided Sept. 8, 1997

Appeals from the United States District Court for the District of Hawaii; David A. Ezra, District Judge, Presiding. D.C. No. CV-91-00725-DAE.

Appeal from the United States District Court for the District of Hawaii; Harold M. Fong, District Judge, Presiding. D.C. No. CV-92-00372-HMF.

Before: HUG, Chief Judge, THOMPSON and O'SCANNLAIN, Circuit Judges.

HUG, Chief Judge:

OPINION

In these consolidated cases we are asked to determine the constitutionality of two land reform ordinances passed by the City Council for the City and County of Honolulu (the "City"). Ordinance 91-95 provides a mechanism for converting leasehold interests in condominium units to fee interests, through the use of the City's condemnation power. Ordinance 91-96 is a rent control measure that limits increases in ground rent due the owner of the land under the condominium units. The trustees of the Bishop Estate ("Bishop Estate") brought an action before District Judge Ezra contesting the constitutionality of both ordinances. The Small Landowners of Oahu ("Small Landowners") brought a separate action before District Judge Fong. Judges Ezra and Fong each entered summary judgments upholding Ordinance 91-95. Judge Ezra also entered a summary judgment holding Ordinance 91-96 (the rent control ordinance) unconstitutional. We have jurisdiction under 28 U.S.C. § 1291 and we affirm.

I. BACKGROUND

Prior to American acquisition, Hawaii developed an extensive feudal land ownership system that has proved remarkably resistant to change. Although Hawaiian leaders and American settlers have repeatedly attempted to divide the large Hawaiian land estates, the results have generally been unsuccessful. As of the late 1980's, the largest eighteen landowners in the state owned 40% of the available land. L.A. Powe, Jr., *Economic Make-Believe in the Supreme Court*, 3 Const. Comm. 385, 389 (1986). The

seventy-two largest landowners owned 47%. *Id.* With the federal and state government owning 49% of the land in the state, *id.*, little is left for the rest of the population. As might be expected in an area of desirable real estate with little land for sale, the price of owning land in Hawaii has grown exponentially over the past several decades.

The large private landowners have adopted a pattern of leasing their land for long terms rather than selling it. Often the land is leased to a developer who builds condominiums[1] on the property. The condominiums are then sold subject to the ground lease. Sometimes the landowners themselves build and sell the condominiums, subject to a ground lease. The leases, commonly for 55 years or longer, require a substantial initial payment and lease payments for 25 to 30 years at a fixed rate. At the end of the initial term, the rent is renegotiated pursuant to the terms of the lease. The new rent usually is based on the market value of the unimproved land as described in the lease. Stated another way, the renegotiated rent is fixed at a percentage of the market value of the parcel underneath the condominium exclusive of improvements (*i.e.*, the condominium).[2] In almost all cases, the renegotiated rent substantially exceeds the initial fixed rate.

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[1] For purposes of this opinion, unless otherwise noted, references to "condominiums" or "condominium properties" include condominium property regime developments, cooperative housing corporation developments, and planned unit developments, which are the three types of developments addressed by Ordinances 91-95 and 91-96.

[2] An example provided by the landowners in their brief is illustrative. The lessees of one apartment purchased their unit in January of 1988 for $986,500, and assumed the existing ground lease. They currently pay $45 per month in ground lease rent

To break up this pattern of land ownership and control the escalating prices of housing, the City passed Ordinances 91-95 and 91-96 on December 18, 1991.

That day the appellants in *Richardson* filed suit in federal court before Judge Ezra seeking declaratory and injunctive relief. The *Richardson* appellants are trustees of the Bishop Estate, a charitable trust established in 1884 under the will of Ke Ali'i Bernice Pauahi Bishop, the great-granddaughter of King Kamehameha I, to erect and maintain schools for indigents and orphans who are native Hawaiians. The Bishop Estate owns the fee simple title to the land underneath condominiums in Honolulu that are affected by the Ordinances.[3] A group of condominium owners calling themselves the Hawaii Leaseholders Equity Coalition (the "HALE Coalition") was granted permission to intervene in the action as an interested party.

On February 14, 1992, the Bishop Estate filed a partial motion for summary judgment. On June 8, 1992, the

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and will continue to do so until the 30-year fixed rent period expires in 1997. At that time, the lease fixes the new rent at six percent of the fair market value of the land exclusive of improvements. If the period had ended in 1991, the parties to the lease might have used the real property tax assessed value used by the City as the fair market value of the land exclusive of improvements. In 1991 the real property tax assessed value used by the City for the land appurtenant to the unit was $213,300. The new ground lease rent would be 6% of that figure, which is $12,798 per year, or $1,066 per month.

[3] The City contends that the Bishop Estate owns approximately 20% of the condominiums on Oahu. The Bishop Estate does not refute this number.

HALE Coalition also moved for partial summary judgment. On June 9, 1992, the City filed a cross-motion for summary judgment on all counts.

Meanwhile, on June 12, 1992, the Small Landowners, a nonprofit membership corporation representing landowners who own smaller plots of land underneath condominium projects, filed a separate complaint in federal court before Judge Fong seeking a declaration that Ordinances 91-95 and 91-96 were constitutionally invalid. The Small Landowners moved to consolidate their action with (or alternatively, to intervene in) the action instituted by the Bishop Estate. The motion was denied and the Small Landowners' suit proceeded separately.

On September 16, 1992, Judge Ezra (1) declared Ordinance 91-96 unconstitutional on its face under the Takings Clause; (2) held that Ordinance 91-95 was facially constitutional under the Public Use, Just Compensation, Due Process, and Equal Protection Clauses of the federal and Hawaii constitutions; and (3) certified to the Hawaii Supreme Court the question whether Ordinance 91-95 was preempted by state law. *See Richardson v. City & County of Honolulu*, 802 F.Supp. 326 (D.Haw.1992).

The Small Landowners and the City subsequently stipulated to dismiss the Small Landowners' claim regarding Ordinance 91-96. The parties also agreed to dismiss the Small Landowners' claims regarding state law preemption, because those questions would be decided by the Hawaii Supreme Court in the *Richardson* case. On September 16, 1993, Judge Fong issued his order holding that Ordinance 91-95 was facially constitutional under the Takings, Due Process, and Equal Protection Clauses of the

federal and Hawaii constitutions, and that the Small Landowners' claims that Ordinance 91-95 failed to provide just compensation or comply with the City's Charter were unripe. *See Small Landowners of Oahu v. City & County of Honolulu*, 832 F.Supp. 1404 (D.Haw.1993).

On February 22, 1994, the Hawaii Supreme Court answered the certified question from *Richardson* in the negative, *Richardson v. City & County of Honolulu*, 76 Hawaii 46, 868 P.2d 1193 (1994), and on April 12, 1994, Judge Ezra adopted the Hawaii Supreme Court's answer. On April 18, 1994, Judge Ezra entered final judgment. Judge Fong entered final judgment in *Small Landowners* on June 20, 1994. All parties filed timely notices of appeal. Because of the similar issues presented, the two actions were consolidated before this court after oral argument.

II. ORDINANCE 91-95

A. The Statute

Ordinance 91-95, which closely parallels Hawaii's Land Reform Act of 1967, creates a mechanism through which condominium owners can convert their leasehold interests into fee simple interests. When at least 25 owners in a condominium complex or the owners of 50% of the units, whichever is less, apply to purchase their leased fee interest, the Ordinance's condemnation procedure is triggered. The Department of Housing and Community Development (the "Department") then determines if the property is proper for condemnation. The Department will begin condemnation proceedings within twelve months unless the owner agrees to voluntarily sell the leased fee interest to the lessees. If the Department

condemns the land, the lessee must purchase the land from the City within 60 days.

In conjunction with enacting the Ordinance, the City made several findings regarding the concentration of land in Honolulu and the effects of such concentration on the local economy. First, the City found that landowners have refused to sell proportionate shares in their fee simple titles and that the few sales that occurred involved exorbitant prices. Honolulu City & County, Haw. Ordinance 91-95, § 1(a). This refusal to sell fee simple titles along with other factors, has caused a dramatic increase in the price of housing in Honolulu. *Id.* The City further found that persons wishing to reside on Oahu were forced to sign long-term leases that provide for periodic rent renegotiation. *Id.* These conditions have led to

> the acute recent inflation of land costs [that] has adversely affected lease rent negotiations of persons who have purchased leasehold multi-family units as their homes: in some instances renegotiations have resulted in lease rents that have increased over 1,000 percent. Under the burden of increased lease rents, many owner-occupants of residential condominium apartments . . . , especially those on fixed incomes, have found, and will continue to find themselves unable to afford to continue living in their homes.

Id. Moreover, the City determined that these defects in the housing market would adversely affect the City's economy:

> There is a close relationship between the monetary values accorded land on Oahu and the stability and strength of Oahu's economy as a

> whole. Residential condominium . . . land values, artificially inflated by concentrated or single ownership, market conditions or other factors, skew Oahu's economy toward unnecessarily high levels. The pervasive and substantial contribution made to inflation by high residential condominium . . . land values creates a potential for economic instability and disruption on Oahu. Economic inflation, instability and disruptions on Oahu have real and potential damaging consequences for all members of an affected society.

Id. The City thus decided to exercise its power of eminent domain to establish a proper real estate market in Honolulu and to reduce the potential for economic instability on Oahu.

B. The Public Use Clause

The Bishop Estate and the Small Landowners (collectively the "landowners") argue that Ordinance 91-95 violates the Public Use Clause of the United States and Hawaii constitutions. The Fifth Amendment of the United States Constitution provides that "private property [shall not] be taken for public use, without just compensation." U.S. Const. amend. V. This provision applies to the states through the Fourteenth Amendment. *See Missouri Pac. Ry. v. Nebraska*, 164 U.S. 403, 417, 17 S.Ct. 130, 135, 41 L.Ed. 489 (1896). Municipalities possessing delegated eminent domain power also are subject to the restrictions of the Fifth and Fourteenth Amendments. *See Chicago B. & Q. R.R. Co. v. City of Chicago*, 166 U.S. 226, 238-39, 17 S.Ct. 581, 585-86, 41 L.Ed. 979 (1896). Similarly, the Hawaii Constitution provides that "[p]rivate property shall not

be taken or damaged for public use without just compensation." Haw. Const. art. I., § 20.

The landowners argue that Ordinance 91-95 is unconstitutional because it takes land for the benefit of private persons and, alternatively, that its public purpose is not served by its mechanism. As noted above, the Ordinance is similar to Hawaii's Land Reform Act of 1967[4] (the "Act"), which was upheld on public use grounds in *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 104 S.Ct. 2321, 81 L.Ed.2d 186 (1984). Because of the Ordinance's similarity to the Act, we begin our analysis with *Midkiff*.

In that case, the Supreme Court upheld the Act, concluding that Hawaii could constitutionally use its power of eminent domain to break up a land oligopoly. *Id.* at 241-42, 104 S.Ct. at 2329-30. The Supreme Court rejected the landowners' arguments that the Act violated the public use requirement of the Taking Clause.[5] The Court stated, "The 'public use' requirement thus is coterminous with the scope of a sovereign's police powers." *Id.* at 240, 104 S.Ct. at 2329.

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[4] The Act was designed to compel large landowners to break up their estates. Under the Act, tenants who lease and live on single-family residential lots within developmental tracts at least five acres in size can ask the Hawaii Housing authority ("HHA") to condemn the property on which they live. When half of the tenants in the tract, or 215 tenants, whichever is less, file an application, the HHA can acquire some or all of the lots in the Act by condemnation. The HHA then can sell the lots to the tenants.

[5] The landowners in *Midkiff* were trustees of the Bishop Estate, the appellants in the *Richardson* action.

Thus, as the Court noted, the judiciary's role in reviewing the legislature's judgment regarding public use is extremely narrow. *Id.* The judiciary should defer to the legislature's public use determination unless the use involves an "impossibility" or is "palpably without reasonable foundation." *Id.* at 240-241, 104 S.Ct. at 2329-30. The Court further noted that "where the exercise of the eminent domain power is rationally related to a conceivable public purpose, the Court has never held a compensated taking to be proscribed by the Public Use Clause." *Id.* at 241, 104 S.Ct. at 2329-30.

Applying that test, the Court noted that the state legislature determined a land oligopoly existed in Hawaii. The Court reasoned that regulating the "oligopoly and the evils associated with it is a classic exercise of a State's police powers." *Id.* at 242, 104 S.Ct. at 2330. Even though the Act's result was to turn land over from one private owner to another, the Court held that the statute's purpose was sufficiently public, *See id.* at 241, 104 S.Ct. at 2329. Finally, the Court noted that using a lease-to-fee transfer statute to regulate that oligopoly was not irrational. *Id.* Accordingly, the Court upheld the Act.

The analysis under the Hawaii Constitution is similarly deferential to the legislature's public use determination.

> [O]nce the legislature has spoken on the social issue involved, so long as the exercise of the eminent domain power is rationally related to the objective sought, the legislative public use declaration should be upheld unless it is palpably without reasonable foundation. The crucial

> inquiry is whether the legislature might reasonably consider the use public, and whether it rationally could have believed that application of the sovereign's condemnation powers would accomplish the public use goal.

Hawaii Housing Authority v. Lyman, 68 Haw. 55, 704 P.2d 888, 897 (1985) (internal citation omitted).

In the present action, both district courts determined that *Midkiff* controlled the outcome of this dispute. Because the statute in *Midkiff* and Ordinance 91-95 are so similar, both courts found no merit in the landowner's public use arguments. Before this court, the landowners seek to distinguish *Midkiff* on several grounds: (1) that the standard of review has changed since *Midkiff;* (2) that the public purpose of the Ordinance is not as compelling as the purpose asserted in *Midkiff;* and (3) that the means of effectuating the purpose is irrational in light of developments since *Midkiff*. We discuss each of these arguments.

1. Change in the standard of review

The landowners argue that, in light of *Dolan v. City of Tigard*, 512 U.S. 374, 114 S.Ct. 2309, 129 L.Ed.2d 304 (1994), *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 112 S.Ct. 2886, 120 L.Ed.2d 798 (1992) and *Nollan v. California Coastal Comm'n*, 483 U.S. 825, 107 S.Ct. 3141, 97 L.Ed.2d 677 (1987), the deference given in *Midkiff* to the legislative body's public use findings is inappropriate.

The landowners assert that those cases require heightened scrutiny. We conclude that those cases are not applicable because they involved uncompensated regulatory takings, in which the issues are quite different.

In a regulatory taking case, the court must determine whether a putative regulatory action masks a taking. For example, in *Dolan*, the most recent case, a shop owner in Oregon brought suit against the City of Tigard. She had applied for a permit needed to expand her store and pave a parking area. *Dolan*, 512 U.S. at 379, 114 S.Ct. at 2313-14. The city's planning commission granted the permit application, but only on the condition that the shop owner dedicate to the city part of her property that was within a floodplain plus a 15 foot strip of land for use as a pedestrian pathway. *Id.* at 379-80, 114 S.Ct. at 2313-14. The shop owner filed suit alleging that the condition was an unconstitutional regulatory taking.

Dolan, as well as *Lucas* and *Nollan*, are quite different from the cases before us. At bottom, those cases involve balancing the authority of state and local governments to engage in land use planning against the property rights of individuals. *See Dolan*, 512 U.S. at 383-86, 114 S.Ct. at 2315-17. The primary issue is whether the landowner is to receive just compensation. *See e.g., id.* at 385, 114 S.Ct. at 2317 ("Under the well-settled doctrine of 'unconstitutional conditions,' the government may not require a person to give up a constitutional right here the right to receive just compensation when property is taken for a public use in exchange for a discretionary benefit conferred by the government where the property sought has little or no relationship to the benefit."). That is, if the Court would have upheld the putative regulatory actions

in those cases, the landowners' property would have been subject to the challenged land restriction and the owner would not have been entitled to compensation for the diminution in land value. The heightened scrutiny applied in *Dolan* thus is necessary to prevent the government from using its regulatory power to force individuals to bear burdens that properly should be born[e] by the public. *See id.*, at 389, 114 S.Ct. at 2319 ("We think this standard is too lax to adequately protect petitioner's right to just compensation if her property is taken for a public purpose.").

Conversely, in the cases before us, the government has expressly exercised its condemnation power and will compensate the landowners. Here, as in *Midkiff*, the requirement of just compensation ensures that individuals will not be forced to bear public burdens, which in all fairness should be borne by the public as a whole. Heightened scrutiny thus is inappropriate. The language used throughout *Midkiff* indicates that deference to the legislative body's public use determination is required when the taking is fully compensated. *See e.g., Midkiff*, 467 U.S. at 241, 104 S.Ct. at 2329-30 ("[W]here the exercise of the eminent domain power is rationally related to a conceivable public purpose, the Court has never held a compensated taking to be proscribed by the Public Use Clause."). For these reasons, we believe that *Nollan-Lucas-Dolan* trio does not signal a change from this long standing rule of deference because we see nothing inconsistent in applying heightened scrutiny when the taking is uncompensated, and a more deferential standard when the taking is fully compensated.

We hold, therefore, that the standard of review to be used in examining Ordinance 91-95 is the minimum scrutiny test espoused in *Midkiff*. We will defer to the City's determination regarding public use unless the use involves an "impossibility" or is "palpably without reasonable foundation." *Midkiff*, 467 U.S. at 240-41, 104 S.Ct. at 2329.

2. The rationality of the public purpose

Unlike the statute at issue in *Midkiff*, the Ordinance is not grounded on the desire of breaking up a land oligopoly. Rather, the City enacted the Ordinance to strengthen Oahu's economy and remedy perceived failures in its real estate market. The City found:

> There is a close relationship between the monetary values accorded land on Oahu and the stability and strength of Oahu's economy as a whole. Residential condominium, cooperative housing and planned development land values, artificially inflated by concentrated or single ownership, market conditions or other factors, skew Oahu's economy toward unnecessarily high levels. The pervasive and substantial contribution made to inflation by high residential condominium, cooperative housing and planned development land values creates a potential for economic instability and disruption on Oahu. Economic inflation, instability and disruptions on Oahu have real and potential damaging consequences for all members of an affected society. Checking inflation, improving the stability of the economy, and avoiding disadvantageous

> economic disruptions all are productive of general benefit to all members of Oahu's community.

Honolulu City & County, Haw. Ordinance 91-95 § 1(a).

This purpose – remedying a failure in the real estate market and strengthening the economy – is a public purpose. *See Midkiff*, 467 U.S. at 242, 104 S.Ct. at 2330 (land oligopoly caused failure in real estate market; regulating evils associated with oligopoly is classic exercise of police power); *Berman v. Parker*, 348 U.S. 26, 75 S.Ct. 98, 99 L.Ed. 27 (1954) (affirming the constitutionality of the District of Columbia Redevelopment Act of 1945, which provided for the condemnation of slum areas for possible sale to private interests). The landowners contend, however, that the evidence presented to the City does not support the stated public purpose. They assert that, contrary to the City's findings, ownership of condominium units is not concentrated in the hands of large landowners and that landowners do sell proportionated shares of their fee simple titles. Thus, they argue that because the City incorrectly determined these facts, the findings do not support the Ordinance's stated public purpose.

Under the standard espoused in *Midkiff*, we must accept the public purpose of the Ordinance unless the City's findings are "palpably without reasonable foundation." *Midkiff*, 467 U.S. at 241, 104 S.Ct. at 2329. The City held three days of public hearings before enacting the Ordinance. The City determined that the price of condominiums was higher because the ownership of the fee simple titles to the land underneath the condominiums

was excessively concentrated. While the hearings produced conflicting testimony, one study presented to the City showed that the largest 20 Landowners own 34.9% of the land under condominium units in Honolulu, and that the largest 60 own 50.4%. Legislative Reference Bureau, Report No. 6, *Ownership Patterns of Land Beneath Hawaii's Condominiums and Cooperative Housing Projects* 21 (1987) (Ownership Patterns). While the largest 20 landowners own a smaller percentage of land underneath condominiums than the largest 22 owned of the fee simple titles when the Court decided *Midkiff*, *see Midkiff*, 467 U.S. at 232, 104 S.Ct. at 2325, the concentration of ownership of land underneath condominiums is greater than the concentration of land ownership throughout the state at the time *Midkiff* was decided. *Compare Ownership Patterns* at 21 (60 persons own 50.4% of land under condominiums), with *Midkiff*, 467 U.S. at 232, 104 S.Ct. at 2325 (72 persons own 47% of land in Hawaii). We thus cannot say that the City's finding is without reasonable foundation.

Similarly, the evidence presented to the City regarding the amount of fee simple lands for sale underneath condominiums was conflicting. We are not free to substitute our judgment for that of the City. The evidence reviewed by the City adequately demonstrated that the land underneath the condominiums was not being sold and that the lack of such sales was driving up the price of housing in Honolulu. We therefore must accept the City's asserted public purpose because its findings are not without reasonable foundation. *See Midkiff*, 467 U.S. at 241, 104 S.Ct. at 2329 ("In short, the Court has made clear that

it will not substitute its judgment for a legislature's judgment as to what constitutes a public use 'unless the use be palpably without reasonable foundation.' ") (citation omitted).

3. The reasonableness of the means used

The landowners also argue that, between 1987 and 1990, the price of condominiums in Hawaii increased by 66%. However, the price of single-family dwellings – which were subject to the Act's lease-to-fee provision – increased by 98%. Dep't of Business and Economic Dev., *The State of Hawaii Databook 1990: A Statistical Abtract* 549 (1990). Thus, the landowners argue that even if a lease-to-fee statute was reasonably related to eliminating a land oligopoly at the time of *Midkiff*, such means are not rationally related to remedying a failure in the real estate market and strengthening the economy in light of recent history.

Deference to the legislative body's public use determination is required " 'until it is shown to involve an impossibility.' " *Midkiff*, 467 U.S. at 240, 104 S.Ct. at 2329 (quoting *Old Dominion Co. v. United States*, 269 U.S. 55, 66, 46 S.Ct. 39, 40-41, 70 L.Ed. 162 (1925)). "Any departure from this judicial restraint would result in courts deciding on what is and is not a governmental function and in their invalidating legislation on the basis of their view on that question at the moment of decision, a practice which has proved impracticable in other fields." *United States ex rel. T.V.A. v. Welch*, 327 U.S. 546, 552, 66 S.Ct. 715, 718, 90 L.Ed. 843 (1946). Additionally, in *Midkiff* the Court noted that whether the statute actually succeeds is irrelevant.

> But "whether in *fact* the provision will accomplish its objectives is not the question: the [constitutional requirement] is satisfied if . . . the . . . [state] Legislature *rationally could have believed* that the [Act] would promote its objective." When the legislature's purpose is legitimate and its means are not irrational, our cases make clear that empirical debates over the wisdom of takings . . . are not to be carried out in the federal courts.

Midkiff, 467 U.S. at 242-43, 104 S.Ct. at 2330 (brackets in original) (quoting *Western & Southern Life Ins. Co. v. State Bd. of Equalization*, 451 U.S. 648, 671-72, 101 S.Ct. 2070, 2084-85, 68 L.Ed.2d 514 (1981)) (internal citations omitted).

Under the rational basis test, we hold that the Ordinance is constitutional under both the United States and Hawaii constitutions. Regardless of what has occurred with single-family dwellings, the City rationally could have believed that, if the supply of condominiums increased (through the lease-to-fee measure of Ordinance 91-95), the price of those condominiums would decrease. Additionally, although the price of single-family houses increased dramatically between 1987 and 1990, there is no indication that the price would not have gone up even more without the Act's lease-to-fee mechanism. Finally, even if the price of condominiums does not decrease as a result of the Ordinance, some of the public purposes of the Ordinance will be served. If a family is allowed to purchase its condominium, that family will not risk being thrown out of its home in 25 years because the family cannot afford the renegotiated rent. The City rationally could have concluded that the lease-to-fee mechanism

would remedy defects in the housing market and stabilize Oahu's economy.

C. The Just Compensation Clause

When a government uses its powers of eminent domain to condemn property, it must provide the property owner with "just compensation." U.S. Const. amend V.; *accord* Haw. Const. art. I, § 20. Just compensation is the "full-monetary equivalent of the property taken." *United States v. Reynolds*, 397 U.S. 14, 16, 90 S.Ct. 803, 805, 25 L.Ed.2d 12 (1970).

The landowners argue that Ordinance 91-95 does not fully compensate them for the taking of their property. In particular, they argue that the Ordinance fails to provide compensation for their loss of rental income or for the diminution in the value of their remaining fee simple interest in any land that is involuntarily converted from their sole ownership to a cotenancy under the ordinance.[6] Both district courts dismissed these claims as unripe. *Richardson*, 802 F.Supp. at 341; *Small Landowners*, 832 F.Supp. at 1411.

Ripeness is a question of law reviewed *de novo*. *Carson Harbor Village Ltd. v. City of Carson*, 37 F.3d 468, 474 (9th Cir.1994). "If a claim is unripe, federal courts lack

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[6] Under the Ordinance, the Department has the option of condemning only a portion of the fee simple title under a condominium project (such as where some of the condominium lessors do not wish to purchase the fee simple title). In such a situation, the original land owner will share the fee simple title to the land with each condominium purchaser as a cotenant.

subject matter jurisdiction and the complaint must be dismissed." *Southern Pac. Transp. Co. v. City of Los Angeles*, 922 F.2d 498, 502 (9th Cir.1990). Whether a claim is ripe generally turns on the fitness of the issues for judicial decision and the hardship to the parties of withholding court consideration. *Pacific Gas & Elec. Co. v. State Energy Resources Conserv. & Devel. Comm'n*, 461 U.S. 190, 201, 103 S.Ct. 1713, 1720, 75 L.Ed.2d 752 (1983). The "central concern [of the ripeness inquiry] is whether the case involves uncertain or contingent future events that may not occur as anticipated, or indeed may not occur at all." 13A Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, Federal Practice and Procedure § 3532 at 112 (2d ed. 1984).

Here, the Bishop Estate came to federal court the same day the City enacted the Ordinance. The condemnation procedure at issue is not self-executing. Rather, several events must occur before any taking will occur. First, at least 25 condominium owners or the owners of 50% of the units, whichever is less, must file an application with the Department to trigger the Ordinance's procedures. Then, after "[d]ue notice is given and a public hearing held," the Department must determine whether the "exercise of the power of eminent domain" requested by the applicants "will effectuate the public purposes of [the Ordinance]." Honolulu City & County, Haw. Ordinance 91-95 § 2.2(a)(2). The Ordinance also requires that, before the Department exercises its power of eminent domain, that the lessor and lessees negotiate "the just compensation which" will be paid. Honolulu City & County, Haw. Ordinance 91-95 § 4.6. Only then will the Department set forth to condemn property.

At this juncture, no group of tenants has asked the Department to invoke the condemnation procedures created by the Ordinance. It is possible that any one of the conditions precedent to the exercise of the Department's eminent domain power might not occur. A sufficient number of qualifying tenants, *see* Honolulu City & County, Haw. Ordinance § 4.4 (setting forth seven requirements that lessee must meet before a sale takes place), might not file an application with the Department. The Department might conclude in any given case that exercising its power of eminent domain would not further the public purpose of the Ordinance. In any event, the required preliminary negotiations could result in an agreement as to the appropriate compensation. Because any one of these contingent events might not occur, we conclude that the landowners' claim under the Just Compensation clause is not ripe for federal adjudication.

The Supreme Court's clear guidance regarding application of the ripeness doctrine to takings claims reinforces our conclusion that the landowners' claim is not ripe. The Court has "placed two hurdles in the way of a takings claim brought in federal court against states and their political subdivisions." *Levald, Inc. v. City of Palm Desert*, 998 F.2d 680, 686 (9th Cir.1993) (internal quotation omitted). It is the second of these two hurdles, which requires that plaintiffs "seek compensation through the procedures the State has provided for doing so before turning to the federal courts," *id.* (internal quotation omitted), that has not been met here. Because no property has been targeted for taking, the landowners have not sought and been denied condemnation [sic] by the Department. Moreover, the landowners have not invoked

the processes provided by Hawaii's courts for obtaining just compensation.

The landowners argue and the dissent concludes, however, that their claims are ripe because the Ordinance's plain language fails to provide for full compensation. Requiring the landowners to seek compensation through Hawaii's procedures, they argue, would be futile under existing state law. *See id.* at 686. The landowners burden of showing that complying with the state's procedures would be futile is a heavy one. *American Savings & Loan Ass'n v. County of Marin*, 653 F.2d 364, 371 (9th Cir. 1981). We conclude that the landowners have not carried their burden.

The Ordinance provides that "[t]he compensation to be paid . . . shall be the current fair market value of the leased fee interest." Honolulu City & County, Haw. Ordinance § 1.2. It defines "leased fee interest" as the "reversionary interests of the fee owner . . . other than the lessee's or sublessee's interest." *Id.* The dissent argues that the plain meaning of the Ordinance deprives the landowners of compensation for the lost stream of rental payments and, therefore, "unless the Ordinance means something other than "what it very clearly says, it does not authorize the Department to give landowners just compensation." *Dissenting Opinion* at 1170. We disagree.

The Ordinance speaks of "reversionary interests" as being in the plural. This points to a recognition of multiple factors to be included in the valuation. The Fifth Circuit has stated that a "reversionary interest is *any* future interest left in a transferor or his successor in interest." *United States v. 50.822 Acres of Land, More or*

Less, 950 F.2d 1165, 1169 n. 4 (5th Cir.1992) (internal quotation omitted) (emphasis added). The Department could well interpret the "reversionary interests" of the fee owner as his entire interest in the land under the condominiums as of the date the eminent domain action is commenced.

Basic principles of property law, in fact, practically compel that interpretation. The reversionary interest of a lessor, as the dissent notes, is "[t]he property that reverts to the grantor after the expiration of an intervening income interest." *Blacks Law Dictionary* 1186 (5th ed. 1979). In other words, a reversionary interest is "[a] right to the future enjoyment of property, at present in possession or occupation of another." *Id.* The Ordinance thus directs the Department to pay the fair market value of the property which reverts to the lessor at the expiration of the lease. What reverts to the lessor is a fee interest in the ground underneath the condominium. The projected earning of that property would be a normal factor in determining the value of the property that reverts to the lessor. *See* Ordinance 91-95 at § 1.2 (defining fair market value as the price to which a willing buyer and seller taking into consideration "all uses to which the land is adapted or might in reason be applied").

We hold that the landowners' challenge is not ripe. There are obviously many different ways the Department could approach the valuation of the lessors' reversionary interest. The Department has not issued regulations regarding the compensation of the landowners and there is no basis for determining that the landowners will not be fully compensated for their interests. It is apparent

that the "plain meaning" of the Ordinance does not foreclose the payment of constitutionally adequate compensation for the landowners' "reversionary interests." Moreover, the City's intent to pay the current fair market value of the leased fee interest is clear. The Ordinance anticipates a complete valuation of the lessors' property interests. It is only if the definition of "leased fee interest" is given a restricted meaning that the landowners would not receive constitutionally adequate compensation. Until that happens, federal adjudication of the landowners' just compensation claim is premature.

D. The Due Process Clause

The Due Process Clause of the Fourteenth Amendment provides that no State shall "deprive any person of life, liberty, or property, without due process of law." U.S. Const. amend. XIV; accord Haw. Const. art I, § 5. The Due Process clause confers both procedural and substantive rights. *United States v. Salerno*, 481 U.S. 739, 746, 107 S.Ct. 2095, 2101, 95 L.Ed.2d 697 (1987); *Armendariz v. Penman*, 75 F.3d 1311, 1318 (9th Cir.1996) (en banc). A municipal act that neither utilizes a suspect classification nor draws distinctions among individuals that implicate fundamental rights will violate substantive due process rights when it is shown that the action is not "rationally related to a legitimate governmental purpose." *Munoz v. Sullivan*, 930 F.2d 1400, 1404 (9th Cir. 1991). We will strike down a statute on substantive due process grounds if it is arbitrary and irrational. *Del Monte Dunes v. City of Monterey*, 920 F.2d 1496, 1508 (9th Cir. 1990).

The landowners again argue that the Ordinance is arbitrary and irrational because it has no legitimate public purpose, because lease-to-fee statutes have been proved not to work, and because the Ordinance is not rationally related to achieving, a valid objective.

The challengers' burden to show that a statute is arbitrary – and irrational is extremely high. *See Del Monte Dunes*, 920 F.2d at 1508. "In a substantive due process challenge, we do not require that the City's legislative acts actually advance its stated purposes, but instead look to whether 'the governmental body could have had no legitimate reason for its decision.' " *Kawaoka v. City of Arroyo Grande*, 17 F.3d 1227, 1234 (9th Cir.1994) (quoting *Levald, Inc.*, 998 F.2d at 690). As explained above, *see supra* section II(B) (2), the City has expressed a valid public purpose in attempting to control condominium price inflation. Furthermore, the City's decision to utilize a lease-to-fee ordinance to effectuate this purpose is not irrational. *See supra* section II(B) (3). Accordingly, we hold that the landowners cannot meet the burden of showing irrationality.

E. The Equal Protection Clause

The United States Constitution guarantees that "[n]o State shall . . . deny to any person within its jurisdiction the equal protection of the laws." U.S. Const. Amend XIV; *accord* Haw. Const. art. I, § 5. The Bishop Estate and the Small Landowners assert that Ordinance 91-95 violates the Equal Protection Clause in two ways. First, the Bishop Estate alleges that ordinance 91-95 was enacted to favor non-Hawaiian lessees over Native Hawaiians and Native

Hawaiian Trusts in violation of their equal protection rights. The Small Landowners additionally allege that the Ordinance violates their equal protection rights by "irrationally grouping together all condominium landowners without any factual or legal basis for inclusion of small landowners."

1. Native Hawaiians' equal protection claims

The Ordinance applies to condominiums regardless of whether the owner is Native Hawaiian or non-Hawaiian. It thus does not on its face draw a distinction on the basis of a suspect classification. Nonetheless, the landowners assert that the Ordinance is unconstitutional due to its discriminatory effects. To prevail, however, the Bishop Estate must show not only a discriminatory effect, but also discriminatory intent. *Village of Arlington Heights v. Metropolitan Housing Dev. Co.*, 429 U.S. 252, 265, 97 S.Ct. 555, 563, 50 L.Ed.2d 450 (1977).

The Bishop Estate introduced no evidence of discriminatory intent on the part of the City. Instead, the Estate alleged that the City must have known that it and other Native Hawaiians owned numerous interests in leased condominiums and therefore that the City was aware the Ordinance would severely affect the Bishop Estate Trust and would harm the interests of Native Hawaiians. We agree with Judge Ezra that these allegations, even if true, do not present a prima facie case of discrimination. It is not enough to show that the City knew the law would affect Native Hawaiians. "Discriminatory purpose . . . implies more than an awareness of consequences." *Personnel Adm'r v. Feeney*, 442 U.S. 256, 279, 99 S.Ct. 2282,

2296. 60 L.Ed.2d 870 (1979). Because the landowners offered no other evidence of discriminatory intent, summary judgment on their equal protection claim was appropriate.

2. Small Landowners' equal protection claim

The Small Landowners contend that the Ordinance violates their equal protection rights by grouping small landowners with owners such as the Bishop Estate, which owns many condominium projects. We disagree.

The Small Landowners do not contend they constitute a suspect class; hence, we will uphold the Ordinance if it is rationally related to a legitimate state interest. *See Massachusetts Bd. of Retirement v. Murgia*, 427 U.S. 307, 312, 96 S.Ct. 2562, 2566, 49 L.Ed.2d 520 (1976). As explained above, the Ordinance furthers a legitimate state interest. See supra section II(B)(2). The Ordinance is rationally related to that interest. *See supra* section II(B)(3). Thus we hold Ordinance 91-95 does not violate the Small Landowners' equal protection rights.

III. ORDINANCE 91-96

A. The Ordinance

As noted above, the land underneath condominiums on Oahu ordinarily is owned by someone other than the owner of the condominium. The condominium owner leases the ground under the condominium, ordinarily for very long terms. In the typical lease, the rent initially is fixed for a term of years, after which the rent is subject to

renegotiation. The renegotiated rent is normally a percentage of the fair market value of the land appurtenant to the unit exclusive of improvements, as of the date of renegotiation. The rapid rise in Hawaiian land prices often results in renegotiated rent several hundred times greater than the initial fixed rent.

Ordinance 91-96 was enacted at the same time as Ordinance 91-95 and essentially is a rent control ordinance. The Ordinance accomplishes its goal in two ways. First, the Ordinance, which applies to all leases that contain provisions for renegotiation of lease rents for owner-occupied condominiums, limits the number and regulates the timing of renegotiations. Section 1.4 of the Ordinance provides that the first renegotiation shall not occur within fifteen years of the initial date of the lease, while subsequent renegotiations shall occur no sooner than every ten years.

Second, the Ordinance caps rents by linking the maximum renegotiated rent to the consumer price index. Section 1.5(b) of the Ordinance limits the renegotiated rent to the initial rent multiplied by a rent factor. The initial rent is the greater of the rent specified by the lease and the reasonable rental value on the effective date of the lease. Honolulu City and County, Haw. Ordinance 91-96. § 1.1. The rent factor is the average consumer price index for the six-month period in which the rent renegotiation divided by the average consumer price index on the date of the initial lease. *Id.* § 1.5(b)(1)-(2).

The Ordinance also contemplates the conveyance of condominiums subject to renegotiated leases on the underlying land. Section 1.10 of the Ordinance facilitates

the conveyance or transfer of these renegotiated leases. That section provides that, if an owner-occupant of a condominium conveys or transfers the leasehold interest in the underlying land during a renegotiated rent period to a person who intends to occupy the condominium apartment, the renegotiated land rent shall apply to the transferee tenant. *Id.* § 1.10. In other words, the owner-occupant of a condominium is free to convey his or her leasehold interest in the underlying land to a person intending to occupy the condominium and the transferee will receive the benefit of the renegotiated land lease. However, if the condominium is conveyed to someone who is not an owner-occupant, the lessor of the underlying land may reopen the negotiation. *Id.* § 1.13.

The Bishop Estate moved for summary judgment, contending that Ordinance 91-96 violates the Takings, Contract and Due Process Clauses. The district court ruled, at summary judgment, that the Ordinance violates the Takings Clause. The district court did not reach the Bishop Estate's Contract and Due Process Clause arguments.

The City and the HALE coalition each filed a timely notice of appeal.

B. The Takings Clause

The Bishop Estate argues that Ordinance 91-96 violates the Takings Clause in two ways. First, the Estate contends that Ordinance 91-96 fails to substantially further its stated public purposes and, therefore, constitutes a regulatory taking because the Ordinance allows a lessee to monetize a below-market renegotiated rent at the

expense of the lessor. Second, the Bishop Estate asserts that the Ordinance violates the Fifth Amendment because it fails to provide for consideration of individualized factors that might affect the value of the lease at the time of renegotiation. The City and HALE Coalition argue that individualized consideration is not necessary and the alleged ground lease premium does not render the Ordinance unconstitutional. We turn to the Bishop Estate's argument that the Ordinance fails to substantially further a legitimate state interest.

A land use regulation, as noted above, does not effect a taking if it substantially furthers a legitimate state interest and does not deny the landowner economically viable use of his land. *Dolan*, 512 U.S. at 385, 114 S.Ct. at 2316-17. Ordinance 91-96 is designed to further the City's interest in maintaining affordable owner-occupied residential housing. Honolulu City & County, Haw. Ordinance 91-96, § 1. The Bishop Estate does not maintain that this is not a legitimate state interest, but rather asserts that the Ordinance fails to substantially further that interest. The Bishop Estate cites *Yee v. City of Escondido*, 503 U.S. 519, 112 S.Ct. 1522, 118 L.Ed.2d 153 (1992) in support of its argument.

Yee involved a rent control ordinance enacted by the City of Escondido that capped the rent a mobile home park owner could charge his lessees. *Yee*, 503 U.S. at 524, 112 S.Ct. at 1526-27. The Yees, owners of two mobile home parks, brought suit alleging that the rent control ordinance violated the Takings Clause. *Id.* at 525, 112 S.Ct. at 1527. They offered two arguments in support of their contention: (1) the rent control ordinance effected a

physical taking of their property; and (2) the ordinance effected a regulatory taking of their property.

The Court did not reach the regulatory taking issue because that question was "not fairly included in the question on which we granted certiorari." *Id.* at 533, 112 S.Ct. at 1531. With respect to their physical taking argument, the Yees relied "heavily on their allegation that the ordinance benefits incumbent mobile home owners without benefiting future mobile home owners, who will be forced to purchase mobile homes at premiums." *Id.* at 530, 112 S.Ct. at 1529. The Court pointed out that this premium effect distinguished the Escondido ordinance from ordinary rent control statutes. Apartment tenants do not sell anything to their successors and, quite often, are statutorily precluded from charging "key money." *Id.* The ordinary rent control ordinance does not allow the lessee to monetize the present value of the reduced rent by conveying an apartment subject to a lease with a below market rent. Although the Court ultimately rejected the Yees' argument because "it has nothing to do with whether the ordinance causes a physical taking," *id.*, it noted that "[t]his effect might have some bearing on whether the ordinance causes a regulatory taking, as it may shed some light on whether there is a sufficient nexus between the effect of the ordinance and the objectives it is supposed to advance." *Id.* (citing *Nollan*, 483 U.S. at 834-35, 107 S.Ct. at 3147-48).

The Bishop Estate makes a similar challenge to Ordinance 91-96. It contends that the Ordinance's conveyance provisions create a premium, which an owner-occupant can capture when she sells a condominium subject to a renegotiated land rent. If the transferee intends to occupy

the condominium, she receives the benefit of the renegotiated rent. Hence, the transferor will charge a premium reflecting the net present value of the difference between the renegotiated land rent and the free market land rent.

The district court found that the Ordinance allowed a lessee to capture the present value of the below market land rent. *Richardson II*, 802 F.Supp. at 338. The Ordinance's failure to regulate resales, according to the district court, effected a transfer of wealth from lessors to lessees. *Id.* Because of this transfer of wealth, which generally does not occur in the ordinary rent control ordinance, the court held that the Ordinance is unconstitutional. While we agree that the Ordinance effects a regulatory taking and, therefore is unconstitutional, we do so for somewhat different reasons than the district court.

The City enacted the Ordinance to provide renegotiated land lease rents "which are affordable to condominium apartment owner-occupants and fair to lessors" and to "maintain [affordable housing] for owner-occupants." The conveyance provision, as explained above, vitiates the cause-and-effect relationship between the property use restricted (rent rates) and the social evil the Ordinance seeks to remedy (lack of affordable housing). Despite this, the City and the Hale Coalition assert that it does not effect an unconstitutional regulatory taking. They assert that all land use regulations increase the value of some property while decreasing the value of other property.

Initially, we must determine whether the Bishop Estate's takings claim is ripe. "There are two independent

prudential hurdles to a regulatory taking claim brought . . . in federal court." *Suitum v. Tahoe Regional Planning Agency*, ___ U.S. ___, ___, 117 S.Ct. 1659, 1664, 137 L.Ed.2d 980 (1997). The first hurdle, that the plaintiff obtain a final decision regarding the application of the regulation to the property at issue from the entity charged with implementing the regulation, *id.* at ___, 117 S.Ct. at 1665, does not apply to facial regulatory takings claims. *Levald*, 998 F.2d at 686. Twice before we have characterized premium based challenges to a rent control statute as facial challenges. *See Carson Harbor*, 37 F.3d at 474 n. 5 ("In *Levald*, which involved similar facts, we noted that the premium is 'relevant only to a facial, not an as-applied, regulatory challenge.' "). The first hurdle thus does not apply to the Bishop Estate's argument.

"The second hurdle stems from the Fifth Amendment's proviso that only takings without 'just compensation' infringe that Amendment; 'if a State provides adequate procedure for seeking just compensation, the property owner cannot claim a violation of the Just Compensation clause until it has used the procedure and been denied just compensation.' " *Suitum*, ___ U.S. at ___, 117 S.Ct. at 1665 (quoting Williamson *County*, 473 U.S. at 195, 105 S.Ct. at 3121 (1985)). Because the Bishop Estate's argument that the Ordinance does not substantially further a legitimate state interest does not depend upon the extent to which the Estate is compensated, its facial regulatory taking claim is ripe. *See Yee*, 503 U.S. at 534, 112 S.Ct. at 1532 ("As this [premium argument] does not depend on the extent to which petitioners are deprived of the economic use of their particular pieces of property or

the extent to which these particular petitioners are compensated, petitioners' facial challenge is ripe."). We therefore turn to the merits of the Bishop Estate's argument.

Land use regulations do influence the value of property, but to be constitutional, they must do so in a manner that substantially furthers a legitimate government interest. *Nollan*, 483 U.S. at 834, 107 S.Ct. at 3147. Ordinance 91-96 does not do this. It regulates the use of the lessors' property interests in a manner that does not substantially further the goal of creating affordable housing. The absence of a mechanism that prevents lessees from capturing the net present value of the reduced land rent in the form of a premium, means that the Ordinance will not substantially further its goal of creating affordable owner-occupied housing in Honolulu. Incumbent owner occupants who sell to those who intend to occupy the apartment will charge a premium for the benefit of living in a rent controlled condominium. The price of housing ultimately will remain the same. The Ordinance thus effects a regulatory taking. *See id.* (regulation must substantially advance a legitimate state interest); *see* also, *Pennell v. San Jose*, 485 U.S. 1, 20, 108 S.Ct. 849, 862, 99 L.Ed.2d 1 (1988) ("Traditional land-use regulation (short of that which totally destroys the economic value of property) does not violate the principle that one should not be forced to bear a burden which belongs to the public as a whole] because there is a cause-and-effect relationship between the property use restricted by the regulation and the social evil that the regulation seeks to remedy.") (Scalia, J., concurring). We accordingly hold

that Ordinance 91-96 violates the Fifth Amendment to the Constitution of the United States.[7]

IV. CONCLUSION

In summary, we hold that Ordinance 91-95 (the lease to fee ordinance) is constitutional. The Ordinance admittedly takes private property, but it does so for a sufficiently public purpose and no constitutional deprivation has as yet been established. Ordinance 91-96 (the rent control ordinance), on the other hand, is unconstitutional because it [fails] to substantially further a legitimate governmental interest. The respective judgments of the district courts are therefore

AFFIRMED.

O'SCANNLAIN, Circuit Judge, concurring in part and dissenting in part.

I join the court's opinion regarding the constitutionality of Ordinance 91-96. With respect to Ordinance 91-95, I concur in the court's conclusion in Part II-B that there is no violation of the Public Use Clause, but write separately to express concern about *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 104 S.Ct. 2321, 81 L.Ed.2d 186 (1984). I respectfully dissent from Part II-C,

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[7] In light of our conclusion that Ordinance 91-96 fails to substantially further a legitimate state interest, we need not reach either the Bishop Estates argument that it fails to provide for consideration of the characteristics of individual lessors or its other arguments.

however, because I believe that the challenge to Ordinance 91-95's compensation provision is ripe, and that the provision does not provide just compensation.

I

In Part II-B the court concludes that Ordinance 91-95 does not violate the Public Use Clause and relies heavily on *Hawaii Housing Authority v. Midkiff.*

A

The Fifth Amendment to the Constitution states: " . . . nor shall private property be taken for public use without just compensation." U.S. Const., amend V. The Public Use Clause is an explicit limit on the power of the government to take private property for, as the Supreme Court has long recognized, a taking must be for public use; a taking for a purely private use is unconstitutional. *See Thompson v. Consolidated Gas Corp.*, 300 U.S. 55, 80, 57 S.Ct. 364, 376, 81 L.Ed. 510 (1937).

Notwithstanding this principle, however, the Supreme Court in *Midkiff* gave the Public Use Clause an exceedingly broad reading: to satisfy the Clause, a taking need only be "rationally related to a conceivable public purpose." *Midkiff*, 467 U.S. at 241, 104 S.Ct. at 2329. "The 'public use' requirement is thus coterminous with the scope of a sovereign's police powers." *Id.* at 240, 104 S.Ct. at 2329; *Nat'l R.R. Passenger Corp. v. Boston & Maine Corp.*, 503 U.S. 407, 422-24, 112 S.Ct. 1394, 1404-05, 118 L.Ed.2d 52 (1992).

Since *Midkiff* was decided, however, the Supreme Court's regulatory takings jurisprudence has undergone considerable change. *See Dolan v. City of Tigard*, 512 U.S. 374, 114 S.Ct. 2309, 129 L.Ed.2d 304 (1994); *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 112 S.Ct. 2886, 120 L.Ed.2d 798 (1992); *Nollan v. California Coastal Comm'n*, 483 U.S. 825, 107 S.Ct. 3141, 97 L.Ed.2d 677 (1987). *Nollan*, *Lucas*, and *Dolan*, of course, dealt with a different area of takings jurisprudence, subject to a different set of rules than the one before us: here we have a challenge under the Public Use Clause whereas that trio dealt with regulatory takings.

Notwithstanding that the *Nollan-Lucas-Dolan* trio dealt with a different part of the Takings Clause, the landowners argue that these cases have modified *Midkiff's* deferential review of a legislature's public use determination. The court rejects this argument, and I agree: the *Nollan-Lucas-Dolan* trio does not expressly modify or overrule *Midkiff*, and therefore we must apply *Midkiff* in this case. Indeed, recent Ninth Circuit authority confirms that *Midkiff* is still viable. *See Bay View, Inc. v. AHTNA, Inc.*, 105 F.3d 1281, 1286 (9th Cir.1997) ("After [*Midkiff*], a legislative determination of what constitutes 'public use' is subject to 'an extremely narrow' review, and will be upheld so long as it's rational."). *Midkiff's* deferential standard compels me to conclude that Ordinance 91-95's taking serves a "conceivable public purpose."

B

Although *Midkiff* has not been overruled, and although *Nollan*, *Lucas*, and *Dolan* deal with a different

part of the Takings Clause, I nevertheless believe that there is tension between these two lines of authority. The underlying thrust of the *Nollan-Lucas-Dolan* decisions increasing the scrutiny of regulations to determine if they go "too far" (enough to require compensation) – is inconsistent with *Midkiff's* sweeping deference. It may be time for the Supreme Court to reconsider *Midkiff.*

To provide the context for this observation, I must take a brief detour. It seems to me that, speaking in broad terms, there are three ways the government can exercise control over property, especially real property. First, it can regulate pursuant to its broad police powers. Second, it can use its power of eminent domain to take the property without the consent of the owner as long as it pays just compensation. Third, it can buy land from a voluntary seller after negotiating a price – that is, it can use its revenues to behave like any other arm's length purchaser of private property. *See* Thomas W. Merrill, *The Economics of Public Use,* 72 Cornell L.Rev. 61, 72 (1986).

Nollan, Lucas, and *Dolan* dealt with the relationship between the first two categories. *Lucas* established when a government regulation goes too far. *See Lucas,* 505 U.S. at 1030, 112 S.Ct. at 2901 ("When . . . a regulation that declares "off-limits" all economically productive or beneficial uses of land goes beyond what the relevant background principle would dictate, compensation must be paid to sustain it."). *Nollan* and *Dolan* tightened the required fit between the legitimate purpose sought to be accomplished by a government regulation and the means chosen – thereby identifying some exercises of the police power as takings. A police power regulation will be treated as a taking – an exercise of eminent domain –

requiring compensation unless it adequately fits its purposes; that is, unless there is an "essential nexus" between a legitimate state interest and the regulation. *See Dolan*, 512 U.S. at 385-87, 114 S.Ct. at 2317; *Nollan*, 483 U.S. at 837, 107 S.Ct. at 3148-49.

The *Nollan-Lucas-Dolan* trio therefore established that the Takings Clause is a limitation upon the state's police powers; if a regulation goes too far, or does not have the right fit, then it must be treated as an exercise of eminent domain – a taking – which requires compensation. The Public Use Clause appears to serve the same sort of function, but with respect to the second and third categories – it limits the state's power of eminent domain. If an exercise of eminent domain goes too far – if it is for a private purpose, not a public one – then it cannot stand. If the state wants to acquire property in such circumstances (and has the statutory authority to do so), it may negotiate with the landowner to purchase the property at an agreed price, but it may not use its condemnation power.[8]

Because the *Nollan-Lucas-Dolan* trio increased the level of scrutiny given to police power regulations, identifying some of them as takings, it stands to reason that the same increased scrutiny should be given to outright condemnation. If a taking does not have the required fit –

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[8] This is not to say that the Public Use Clause prohibits the government from possessing property for a non-public use; if the government with the statutory power to do so purchases the property from a voluntary seller, there is no taking at all because there is no use of eminent domain. The government becomes the owner with the consent of the seller.

perhaps something like *Nollan's* "essential nexus" – between its proclaimed public use and its actual effect, then it should be invalid under the Public Use Clause.

The court's opinion seeks to distinguish these cases, but I am unpersuaded. To the majority, the distinction is the provision of compensation: "[W]e see nothing inconsistent in applying heightened scrutiny when the taking is uncompensated, and a more deferential standard when the taking is fully compensated." Whereas the majority is correct that there is less reason to be suspicious of a fully compensated taking than an uncompensated one, more deference does not imply absolute deference. We ought not vitiate the public use requirement because, even if a landlord does receive the "fair market value" of the property, the landlord loses his right to exclude. Whether because of a sentimental attachment to his property or a conviction that the property is actually worth more than what the market will currently bear, a landlord might choose not to sell, even at the "fair market value." The landlord who refuses to sell is asserting his right to exclude. As the *Dolan* Court recognized, "th[e] right to exclude others is 'one of the most essential sticks in the bundle of rights that are commonly characterized as property.' " *Dolan*, 512 U.S. at 393, 114 S.Ct. at 2320 (quoting *Kaiser Aetna v. United States*, 444 U.S. 164, 176, 100 S.Ct. 383, 391, 62 L.Ed.2d 332 (1979)). The public use requirement protects this right by limiting government encroachment on private property – by forcing the government to prove that it is upholding the public welfare and not merely transferring wealth to a class of persons with a stronger political voice.

Therein lies the mischief of *Midkiff*. Hopefully the Supreme Court will have the opportunity to extend its emerging takings jurisprudence to protect the right to exclude and to add vitality to the public use requirement. If the Clause is to have any effect at all, it must mean that a court will not feign blindness when it sees through a patently transparent legislative recital that a taking is for a public use. When the government uses eminent domain to take real property from A and give it to B, with no meaningful impact on anyone else or on the community at large, the taking is purely private and should violate the Public Use Clause.

In my view, Ordinance 91-95, unlike the statute in *Midkiff*, is a purely private taking. In *Midkiff*, the legislature was attempting to break up an oligopoly in land ownership remnant of Hawaii's feudal past – to allow single family home ownership. Breaking apart large blocks of land held by a small group of landowners – blocks which encompassed almost half the entire State of Hawaii could be reasonably expected to spark more land transactions and lead to a more fluid real estate market. *See Midkiff*, 467 U.S. at 232-33, 104 S.Ct. at 2324-25. That some economists might disagree with the legislature's remedy does not mean that the statute would be invalid – it retained an "essential nexus" to its purpose and would be constitutional.

In this case, however, the Honolulu City Council found no land oligopoly, but a mere concentration of land ownership in the hands of landowners (a tautology), many of whom refused to sell their land to their leasehold tenants (typically groups of high-rise condominium owners), which in turn led to increased real property

prices. As a remedy, when properly triggered, Ordinance 91-95 would condemn the property of the landowners and transfer it in pro rata shares to the condominium owners. It seems to me that the ordinance is nothing more than a naked transfer from one property owner to another from landlords to tenants. To be sure, because tenants will be able to own land that they could not purchase in the open market, the ordinance might well make today's tenants better off, and will certainly eliminate their need to pay rent altogether. But transferring title to the tenants will not change the value of the property which will still equal the combined value of the leasehold interest and the reversionary interest and hence should not lower the price a seller will demand. If the landlords constituted an oligopoly, then the division of the ownership of the land could have the effect of lowering land prices from an oligopolistic level to something approaching the free-market level. In the absence of a showing of an oligopoly, however, Ordinance 91-95 has nothing to do with changing the structure of Hawaii's real estate market.

Nevertheless, *Midkiff*'s language limits the public use inquiry to whether there is a conceivable public purpose behind the law. Applying that deferential standard, I conclude that Ordinance 91-95 barely passes muster, and therefore I reluctantly concur in the court's conclusion that it does not violate the Public Use Clause.

II

In Part II-C of its opinion, the court concludes that the landowners' compensation claims are not ripe. It does

so while theoretically recognizing the well-established rule that a party need not seek compensation when doing so would be futile under existing state law. *See Levald, Inc. v. City of Palm Desert*, 998 F.2d 680, 686 (9th Cir. 1993); *see also Williamson County Regional Planning Comm'n v. Hamilton Bank*, 473 U.S. 172, 196-97, 105 S.Ct. 3108, 3121-22, 87 L.Ed.2d 126 (1985).

Ordinance 91-95 sets the compensation for the taking as "the current fair market value of the leased fee interest." Ordinance 91-95, § 5.3. It defines the "leased fee interest" as the "reversionary interests of the fee owner." *Id.* at § 1.2.

By its plain meaning, the ordinance pays only the current fair market value of the landowner's reversionary interest. In other words, the landowner gets paid only for his interest in the property which excludes the leasehold. Conspicuously absent from this formula is any payment for the current stream of rental payments from the tenants to the landlord. Undoubtedly, the landlord has a protected property interest in the rental payments – a lessor's interest distinct from the reversionary interest in the land. Currently, the tenants pay rent to the landlord for the lease term. Under the ordinance, the tenants stop paying rent immediately upon condemnation. The landlord loses the stream of payments for the leasehold period but is not compensated for the loss.

In the court's view, Honolulu's Department of Housing and Community Development could interpret the compensation provision broadly and include the lost rental payments in the compensation formula. I do not think a fair (or even generous) reading of the ordinance

will sustain that conclusion. The ordinance is clear: the landowners will get paid only for their "reversionary interests," which, as a matter of basic property law, do not include the current income from the property. *See Black's Law Dictionary* 1186 (5th ed. 1979) (defining "reversionary interest" as "[t]he property that reverts to the grantor after the expiration of an intervening income interest"). The Supreme Court has recognized that merely compensating a lessor for the reversionary interest is insufficient:

> "[W]hen a lease of trust land is made. . . . upon a subsequent condemnation by the United States, the trust must receive the then full value of the reversionary interest that is subject to the outstanding lease, *plus, of course, the value of the rental rights under the lease.*"

Alamo Land & Cattle Co., Inc. v. Arizona, 424 U.S. 295, 303, 96 S.Ct. 910, 916, 47 L.Ed.2d 1 (1976) (emphasis added). The landlord must receive the value of the leased payments because that is the difference between what is taken by the government (a present fee simple) and the fair market of the "reversionary interests."

The court reaches the incorrect result because its analysis is incomplete. After noting that what reverts back to the landlord is a fee interest, the court states that "[t]he projected earning of that property would be a normal factor in determining the value of the property that reverts to the lessor." The court is correct in that what reverts back is a fee interest, and that the value of a fee interest takes into account all projected earnings. The court does not recognize, however, that a reversionary interest in fee simple is a lesser estate than a present fee

simple, and that the difference is the interim lease payments. One can view the value of property as the sum of the discounted *future* cash flows. A reversionary interest is less valuable than a present fee simple because the value of a reversionary interest does not include the rent payments made prior to reversion, as those would be *past* cash flows.

Thus, to provide just compensation, Hawaii must pay the landlords the value of the reversionary interest plus the present value of the lease payments. There is no need to wait and see how the Department administers Ordinance 91-95, for unless the ordinance means something other than what it very clearly says, it does not authorize the Department to give landowners just compensation. In light of the plain meaning of the ordinance, any compensation paid by Honolulu to the landowners would be constitutionally inadequate. The formality of pursuing such compensation would therefore be futile. For that reason, I would conclude that the landowners' compensation claims are ripe for review, and that the district court's order should be reversed to that extent.

APPENDIX B

UNITED STATES DISTRICT COURT
D. HAWAII

Civ. No. 91-00725 DAE

WILLIAM S. RICHARDSON, *et al.*,

Plaintiffs,

V.

CITY AND COUNTY OF HONOLULU,

and Defendant,

HALE COALITION,

Intervenor.

Sept. 16, 1992

ORDER GRANTING IN PART AND DENYING IN PART MOTIONS FOR SUMMARY JUDGMENT AND CERTIFYING QUESTION TO HAWAII SUPREME COURT

DAVID ALAN EZRA, District Judge.

This court heard the parties' motions for summary judgment on August 10, 1992.

BACKGROUND

On December 4, 1991, the City Council of defendant City and County of Honolulu[1] passed Bills 156 (1990) and

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[1] The court will refer to the City and County of Honolulu as "Honolulu" when discussing the geographical location and as "the City" when addressing the defendant political entity.

36 (1991) which were later enacted on December 18, 1991 as Ordinances 91-95 and 91-96, respectively. Ordinance 91-95 involves a mechanism for the transfer of the fee simple interest of leasehold property from condominium lessors to condominium lessees in Honolulu. Ordinance 91-96 imposes a ceiling on renegotiated lease rents for ground leases of owner-occupied residential condominium units in Honolulu.

On December 18, 1991, the date of enactment of the aforementioned ordinances, the plaintiff Trustees of the Kamehameha Schools/Bernice Pauahi Bishop Estate ("Bishop Estate") filed the present action alleging that both ordinances are unconstitutional. Bishop Estate asserts, the following specific causes of action:

> Count I – Deprivation of constitutional rights in violation of 42 U.S.C. § 1983;
>
> Count II – Ordinance 91-96 is facially unconstitutional in that it effects an impermissible taking in violation of the Fifth and Fourteenth Amendments;
>
> Count III – Ordinance 91-96 is facially unconstitutional. In that it violates Bishop Estate's substantive due process rights under the Fifth and Fourteenth Amendments;
>
> Count IV – Ordinance 91-96 is facially unconstitutional in that it violates Bishop Estate's procedural due process rights under the Fourteenth Amendment;
>
> Count V – Ordinance 91-96 is facially unconstitutional in that it violates Bishop Estate's equal protection rights under the Fourteenth Amendment;

Count VI – Ordinance 91-96 unreasonably and substantially impairs Bishop Estate's contract rights in violation of Article I, Section 10 of the Constitution;

Count VII – Ordinance 91-95 is facially unconstitutional in that it effects an impermissible taking in violation of the Fifth and Fourteenth Amendments;

Count VIII – Ordinance 91-95 is facially unconstitutional in that it violates Bishop Estate's substantive due process rights under the Fifth and Fourteenth Amendments;

Count IX – Ordinance 91-95 is facially unconstitutional in that it violates Bishop Estate's equal protection rights under the Fourteenth Amendment;

Count X – Ordinance 91-96 violates several provisions of the Constitution of the State of Hawaii;

Count XI – Ordinance 91-95 violates several provisions of the Constitution of the State of Hawaii;

Count XII – Ordinance 91-96 conflicts with various statutes of the State of Hawaii; and

Count XIII – Ordinance 91-95 conflicts with various statutes of the State of Hawaii.

Bishop Estate seeks declaratory relief as well as attorneys' fees, costs, and interest.

On February 14, 1992, Bishop Estate filed a motion for partial summary judgment on Counts I, II, III, VI, XII, and XIII. On June 8, 1992, the HALE Coalition filed a motion for partial summary judgment on the remaining

counts of the complaint. On June 9, 1992, the City filed a cross motion for summary judgment on all counts.

DISCUSSION

V. ORDINANCE 91-96

A. BACKGROUND

Ordinance 91-96 imposes a ceiling on renegotiated lease rents for ground leases of owner-occupied residential condominium units in Honolulu. In the "Findings and Purpose" section of Ordinance 91-96, the City found that there were 25,203 owner-occupied condominium housing units in Honolulu in 1987. Ord. 91-96 § 1(1)(A). The City further found that 16,291 of such units, or approximately 65% of the total, were on leased land.[2] *Id.* § 1(1)(B). The City indicated that residential leaseholds have had, and continue to have, numerous undesirable socio-economic effects including: increases in lease rental negotiations of up to 1,000%; inequality of bargaining power favoring lessors; and increasing lease rentals forcing lessees to give up their leases and look for other accommodations. In sum, the City stated:

> The purpose of this Ordinance is to set maximum renegotiated lease rents which are affordable to condominium apartment owner-occupants and fair to lessors. This Ordinance is intended to be in conformance with *[Richardson I]*.[3]

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[2] The City indicated that it had no reason to believe that this data had changed appreciably since 1987. Ord. 91-96 § 1(2).

[3] In *Richardson v. City and County of Honolulu*, 759 F.Supp. 1477 (D.Haw.1991) (*"Richardson I"*), this court declared

Ordinance 91-96 applies to all leases that contain provisions for renegotiation of lease rents for individual residential owner-occupant apartments. Ord. 91-96 § 1.3. An "owner-occupant" is defined as an owner of a residential apartment who, on the date of renegotiation of the lease of the residential apartment, occupies the residential apartment as the owner's principal residence. *Id.* § 1.2(a). Pursuant to the ordinance, the first renegotiation shall not be scheduled before the fifteenth year following the initial date of the lease and subsequent renegotiations shall occur no more frequently than every ten years. *Id.* § 1.4(a)(1).

Ordinance 91-96 provides that the maximum annual renegotiated lease rent shall be the initial lease rent multiplied by a rent factor. *Id.* § 1.5(b). The "initial lease rent" is the greater of the beginning lease rent specified in the lease or the reasonable market value rent prevailing at the effective date of the lease.[4] *Id.* § 1.1. Furthermore, the "rent factor" is the average consumer price index ("CPI")[5] for the six-month period in which the rent negotiation occurs divided by the average CPI in effect at the

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unconstitutional Ordinance 91-96's predecessor, Ordinance 90-95. *Richardson I* is discussed at length later in this opinion.

[4] In the definition of "initial lease rent," the ordinance states that initial lease rent "excludes any lease rents that reflect reduced rent at the beginning of the lease due to construction of the project or due to special negotiations between the developer and the land owner." Ord. 91-96 § 1.1.

[5] CPI is defined as "the Consumer Price Index for All Urban Consumers (CPI-U) for Honolulu published by the Bureau of Labor Statistics of the United States Department of Labor." Ord. 91-96 § 1.1.

time of the effective date of the initial lease rent. *Id.* § 1.5(b).

When a lease comes up for renegotiation, the lessor and lessee are encouraged to attempt to reach agreement as to the renegotiated lease rent. *Id.* § 1.4(b). If the parties are unable to reach an agreement, however, they must proceed to arbitration. *Id.* If the lease at issue is subject to section 516D-12 of the Hawaii Revised Statutes, the arbitration shall proceed pursuant to chapter 516D. *Id.* Otherwise, the City Department of Housing and Community Development (the "Department") shall arbitrate the matter. *Id.* The Department is also charged with enforcing the provisions of Ordinance 91-96. *Id.* § 1.14.

Ordinance 91-96 also provides a mechanism for adjusting the renegotiated lease rent biennially in order to account for further changes in the CPI. *Id.* § 1.6. Furthermore, under certain narrowly-defined circumstances, the ordinance allows for an administrative adjustment of annual renegotiated lease rent to an amount higher than the maximum annual renegotiated lease rent. *Id.* § 1.7. In general terms, a lessor may petition the Department for an administrative adjustment when the lessor pays the operating expenses from lease rent proceeds and the lessor's current net operating income is less than the lessor's net operating income in the last year of the fixed rent period. *Id.* § 1.7(c). When authorized, the lease rent shall be adjusted so that the net operating income, as adjusted for inflation measured by the CPI, stays the same as the net operating income in the last year of the fixed rent period. *Id.* § 1.7(b), (c). Either the lessor or lessee may appeal the Department's approval, or modification of a proposed adjusted lease rent. *Id.* § 1.7(g).

Every renegotiated lease rent, whether set by agreement or arbitration, must be submitted to the Department for certification that the rent is within the applicable maximum. *Id.* § 1.9. The renegotiated lease rent shall be deemed within the maximum unless, within thirty days of the submission of the renegotiated lease rent, the Department certifies that such rent is not within the maximum. *Id.* § 1.9(d). If the Department rejects the proposed renegotiated lease rent, the lessor and lessee must continue their renegotiation. *Id.*

Any party aggrieved by the Department's action or inaction may appeal to the Department. *Id.* § 1.9(e). Upon the filing of an appeal, the Department shall (1) hold a hearing in accordance with the contested case procedures of Chapter 91 of the Hawaii Revised Statutes, and (2) issue an appropriate decision.[6] *Id.*

If an owner-occupant transfers his leasehold interest during a renegotiated rent period to another person intending to be an owner-occupant, the renegotiated lease rent shall be applicable to the new owner-occupant. *Id.* § 1.10. However, if an apartment owner ceases to be an owner-occupant or if an owner-occupant transfers his

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[6] The drafters of Ordinance 91-96 apparently attempted to take into account the potential conflict between Hawaii Revised Statutes chapter 658 which governs the finality of arbitration awards and section 1.9 of Ordinance 91-96. Section 1.9(f) provides that if a court of competent jurisdiction rules, or the state attorney general or corporation counsel opines, that a renegotiated lease rent set by arbitration may be vacated, modified, or corrected only pursuant to chapter 658, then a petition seeking such action shall be subject to chapter 658 and the parties may not appeal to the Department.

leasehold interest to a person who is not an owner-occupant, the lessor may reopen the negotiated lease rent. *Id.* § 1.12, 1.13. Once reopened, the renegotiated lease rent must be set in accordance with the lease agreement and without regard to the provisions of Ordinance 91-96. *Id.*

B. THE TAKINGS CLAUSE (COUNT II)

1. Richardson I

In *Richardson v. City and County of Honolulu*, 759 F.Supp. 1477 (D.Haw.1991) ("*Richardson I*"), this court considered the constitutionality of Ordinance 91-96's statutory predecessor, Ordinance 90-95. This court held that Ordinance 90-95 violated the Takings Clause of the United States Constitution. As the City drafted Ordinance 91-96 so as to attempt to correct the constitutional deficiencies of Ordinance 90-95, it is necessary to review *Richardson I*.

Ordinance 90-95 was designed to impose a maximum ceiling on renegotiated lease rents for residential condominiums in Honolulu. The ordinance provided that the renegotiated annual ground rent shall not exceed the initial lease rent paid at the beginning of the lease term multiplied by a "rent factor." *Richardson I*, 759 F.Supp. at 1479. The rent factor was an average of an "inflation factor" and an "income factor." *Id.* The lessors were bound by the rent figure determined by this formula regardless of whether the initial rent paid by the lessee reflected the market value of the property at the time the lease began. *Id.* at 1480.

The court further explained:

> The maximum renegotiated rents mandated by the Ordinance apply for the full renegotiated rent period and are not readjusted to reflect changes in the [indexes for the inflation and income factors] which might occur during that time. The Ordinance does not take into consideration the location or any other unique or particular characteristics of the property. There is no administrative procedure for appeal, and no governmental body has been established or designated in the Ordinance for the purpose of interpreting and applying the Ordinance's provisions.

759 F.Supp. at 1480.

The court held that Ordinance 90-95 was unconstitutional under the Fifth Amendment's Takings Clause because: (1) the ordinance did not allow lessors a reasonable rate of return; and (2) the ordinance's means did not rationally further its public purpose.

The court found that Ordinance 90-95 on its face deprived lessors of a just and reasonable rate of return because the rent ceiling was based on the amount of rent paid by the lessee during the first year of the lease. 759 F.Supp. at 1489. The undisputed evidence in the case showed that the rent paid by lessees during the first year of their leases was often far below market value. *Id.* at 1490. The court further determined that Ordinance 90-95 was unconstitutional because it did not provide a mechanism for periodic review of the rent ceilings imposed in order to ensure that lessors are continuously afforded a fair rate of return. *Id.* at 1491.

Additionally, while the court found that Ordinance 90-95 had a legitimate public purpose, it determined that the ordinance did not reasonably further the ordinance's goal of reducing the cost of leasehold housing for the people of Hawaii. 759 F.Supp. at 1493. The evidence in the case demonstrated that the ordinance applied to numerous types of condominiums which are not rented by lessees seeking residential housing. *Id.* at 1494. In fact, the evidence showed that only about 37% of all residential leasehold condominiums on Oahu were owner-occupied. As Ordinance 90-95 applied only to renegotiated annual ground rents, the court noted that it was inapplicable to sublessees who are the majority of the occupiers of condominiums.

The court summarized the problems of Ordinance 90-95 as follows:

> To the extent that the drafters intended to provide renters with more affordable housing, the approach chosen by the drafters of Ordinance 90-95 is not constitutionally rational. First, the Ordinance does not place any restrictions on rents charged to occupants by sublessors. Second, the terms of the Ordinance apply not only to residential condominiums but also to commercial condominiums. Third, the Ordinance does not take into consideration the individual characteristics or market value of any piece of property in determining the maximum allowable renegotiated rent. Finally, no governmental agency has been designated to interpret the Ordinance, oversee its application, or evaluate whether the rent ceiling is reasonable in every case.

759 F.Supp. at 1494.

While the court determined that Ordinance 90-95 was unconstitutional, the court noted:

> Careful review and analysis of constitutional law and precedent convinces this court that a properly crafted ordinance, the purpose of which is to limit lease rent increases, can pass constitutional muster. . . . This court *does* not hold that *every* effort to regulate rent renegotiations would be unconstitutional. Rather, the court finds that *this particular ordinance is* unconstitutionally overbroad.

Id. at 1479, 1488.

2. General Taking Analysis

The Takings Clause of the Fifth Amendment to the United States Constitution states that "private property [shall not] be taken for public use, without just compensation." The Takings Clause applies to the states through the Fourteenth Amendment. *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 244 n. 7, 104 S.Ct. 2321, 2331 n. 7, 81 L.Ed.2d 186 (1984). Moreover, a state may delegate its power to condemn to a municipality. Cf. *Jacobson v. Tahoe Regional Planning Agency*, 566 F.2d 1353 (9th Cir.1977), *aff'd in part and rev'd in part on other grounds*, 440 U.S. 391, 99 S.Ct. 1171, 59 L.Ed.2d 401 (1979). "When the power to condemn has been delegated to a municipality, the municipality acts under color of state law, and therefore the prohibitions of the fifth and fourteenth amendments apply." *Richardson I*, 759 F.Supp. at 1487.

The Supreme Court has consistently distinguished "physical takings" from "regulatory takings." A physical

taking occurs when a governmental entity authorizes a permanent physical occupation of real property. On the other hand, the regulatory taking issue typically arises when a government regulation, such as a zoning regulation or a rent control law, affects a property owner's ability to use his land. The distinction between a physical taking and a regulatory taking is significant because the Supreme Court has applied vastly different standards to the two types of takings.

3. Physical Taking

The Supreme Court addressed at length the issues regarding a physical taking in *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982). In that case, the defendant cable television company installed a cable on the roof of the plaintiff's apartment building. The company's actions were in accordance with a New York law which required a landlord to permit a cable television company to install its cable facilities upon his property. The issue in the case was "whether a minor but permanent physical occupation of an owner's property authorized by government constitutes a 'taking' of property for which just compensation is due under the Fifth and Fourteenth Amendments of the Constitution." *Id.* at 421, 102 S.Ct. at 3168. The Supreme Court held that any permanent physical occupation constitutes a per se taking thereby requiring just compensation. *Id.* at 426-441, 102 S.Ct. at 3170-79.

The instant case does not involve an actual permanent physical occupation as was present in *Loretto*. Nonetheless, Bishop Estate relies on a series of decisions from

the courts of appeals which held that certain mobile home park rent control ordinances effected "physical takings," similar to the type of taking in *Loretto*. These ordinances allegedly transferred possessory rights in the mobile home park from the owners to the tenants by essentially giving tenants a transferable right to a perpetual lease at below-market rental rates. *See Azul Pacifico, Inc. v. City of Los Angeles*, 948 F.2d 575 (9th Cir.1991), *opinion withdrawn on other grounds*, 973 F.2d 704 (9th Cir. 1992);[7]

Pinewood Estates v. Barnegat Township Leveling Bd., 898 F.2d 347 (3d Cir.1990); *Hall v. City of Santa Barbara*, 833 F.2d 1270 (9th Cir.1986), *cert. denied*, 485 U.S. 940, 108 S.Ct. 1120, 99 L.Ed.2d 281 (1988).

The physical taking analysis in the aforementioned cases, however, was overruled by the Supreme Court's recent opinion in *Yee v. City of Escondido*, ___ U.S. ___, 112 S.Ct. 1522, 118 L.Ed.2d 153 (1992). In *Yee*, the plaintiff mobile home park owners challenged a local mobile home park rent control ordinance. The park owners alleged that the ordinance constituted a physical taking

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[7] In *Azul-Pacifico*, the Ninth Circuit granted a petition for rehearing and withdrew its previous decision reported at 948 F.2d 575. On rehearing, the court did not address the takings clause issues, but it vacated the lower court's judgment on other grounds. In particular, the court held: (1) the plaintiff could not bring a direct constitutional claim without utilizing 42 U.S.C. § 1983; and (2) the claims were barred by the statute of limitations.

under *Loretto*.[8] Rejecting the owners' arguments, the Supreme Court held that a physical taking occurs only when the government requires the landowner to submit to the physical occupation of his land. *Id.* 112 S.Ct. at 1529. The Court emphasized that the mobile home park owners voluntarily rented their land to the tenants; the park owners' tenants were invited by the park owners, not forced upon them by the government. *Id.* The Court explicitly rejected the rationale of *Hall* and *Pinewood Estates*. *Id.* at 1527 ("We granted certiorari . . . to resolve the conflict between the decision below [dismissing the

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[8] The Court summarized plaintiffs' argument as follows:

> Because under the California Mobilehome Residency Law park owner cannot evict a mobile home owner or easily convert the property to other uses, the argument goes, the mobile home owner is effectively a perpetual tenant of the park, and the increase in the mobile home's value thus represents right to occupy a pad at below-market rent indefinitely. And because the Mobilehome Residency Law permits the mobile home owner to sell the mobile home in place, the mobile homeowner can receive a premium from the purchaser corresponding to this increase in value. The amount of this premium is not limited by the Mobilehome Residency Law or the Escondido ordinance. As a result, petitioners conclude, the rent control ordinance has transferred a discrete interest in land – the right to occupy the land indefinitely at a sub-market rent – from the park owner to the mobile home owner. Petitioners contend that what has been transferred from park owner to mobile home owner is no less than a right of physical occupation of the park owner's land.

112 S.Ct. at 1528.

complaint] and those of two of the federal Courts of Appeals in *Hall* [and *Pinewood Estates.*]).

Additionally, the Court found that the factual circumstances in *Yee* were similar to the case of *FCC v. Florida Power Corp.*, 480 U.S. 245, 107 S.Ct. 1107, 94 L.Ed.2d 282 (1987). In that case, the plaintiff utility company leased space on its utility poles to cable television companies for the installation of cables. Pursuant to federal agency action, the annual rent of several cable companies was reduced from between $7.15-$5.50 per pole to $1.79 per pole annual rent. Rejecting the utility's physical taking argument, the Supreme Court explained:

> [The utility contends,] in essence, that it is a taking under *Loretto* for a tenant invited to lease at a rent of $7.15 to remain at the regulated rent of $1.79. But it is the invitation, not the rent, that makes the difference. The line which separates these cases from *Loretto* is the unambiguous distinction between a commercial lease and an interloper with a government license.

Pursuant to the Supreme Court's holdings in *Florida Power* and *Yee*, this court finds that there is no physical taking in the present case. In support of their physical taking allegation, Bishop Estate relies almost entirely on *Hall*, *Pinewood Estates*, and *Azul-Pacifico*. Yet the physical taking rationale of these cases was specifically rejected in *Yee*. Moreover, the condominium lessees in the present case are entirely analogous to the tenants in *Florida Power* and *Yee*. The lessees are occupying their condominiums as a result of leases extended by the lessors, not as a result of governmental mandate. The City did not require the lessors to be subject to physical occupation of their land.

4. Regulatory Taking

a) Applicable Law

The long-standing rule regarding regulatory takings was enunciated by Justice Holmes: "while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking." *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 415, 43 S.Ct. 158, 160, 67 L.Ed. 322 (1922). With respect to the regulation of housing, the Supreme Court has indicated:

> This Court has consistently affirmed that States have broad power to regulate housing conditions in general and the landlord-tenant relationship in particular without paying compensation for all injuries that such regulation entails. . . . So long as these regulations do not require the landlord to suffer the physical occupation of a portion of his building by a third party, they will be analyzed under the multifactor inquiry generally applicable to non-possessory governmental activity.

Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419, 440, 102 S.Ct. 3164, 3178, 73 L.Ed.2d 868 (1982) (citing, among others, the following two rent control cases: *Bowles v. Willingham*, 321 U.S. 503, 64 S.Ct. 641, 88 L.Ed. 892 (1944); and *Block v. Hirsh*, 256 U.S. 135, 41 S.Ct. 458, 65 L.Ed. 865 (1921)).

The seminal case regarding regulatory takings is *Penn Cent. Transp. Co. v. City of New York*, 438 U.S. 104, 98 S.Ct. 2646, 57 L.Ed.2d 631 (1978). In that case, pursuant to

the City of New York Landmarks Preservation Law,[9] the Grand Central Terminal ("Terminal"), owned by plaintiff Penn Central Transportation Company ("Penn Central"), was designated as a historical landmark. After Penn Central's proposal to build a 55-story office building on top of the Terminal was rejected,[10] it filed suit alleging that the application of the Landmarks Preservation Law to the terminal constituted a "taking" in violation of the Fifth and Fourteenth Amendments.

The Supreme Court held there was no taking. The Court explained that the taking analysis involves essentially ad hoc, factual inquires involving several factors. 438 U.S. at 124, 98 S.Ct. at 2659. The Court indicated that a court must consider the economic impact of the regulation on the plaintiff, the extent to which the regulation has interfered with distinct investment-backed expectations, and the character of the government action. *Id.*

The Supreme Court rejected Penn Central's argument that the Landmarks Preservation Law effected a taking because its operation significantly diminished the value

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[9] The City of New York enacted the Landmarks Preservation Law which created a commission having the power to designate historic landmarks in New York City. Once a site is designated as a landmark numerous restrictions attach to the property owner's use of the property. In order to partially offset the effect of these restrictions, landmark owners who have not developed their property to the extent otherwise allowed by the general zoning laws are allowed to transfer their development rights to other parcels in the vicinity. 438 U.S. at 109-114, 98 S.Ct. at 2651-54.

[10] Penn Central would have received $1-3 million annually from the proposed project.

of the Terminal site. 438 U.S. at 131, 98 S.Ct. at 2662. Of particular importance, the Court noted that Penn Central had conceded that the parcel of land occupied by the Terminal was, at the time of the lawsuit, capable of earning a reasonable return. *Id.* at 129, 98 S.Ct. at 2661. Accordingly, the Court held that while the Landmark Preservation Law undeniably interfered with Penn Central's profit-making ability, the law still afforded Penn Central a reasonable return on its investment. 438 U.S. at 136-37, 98 S.Ct. at 2665-66.

While *Penn Central* provides the general framework for evaluating a regulatory taking claim, subsequent federal and state cases have refined the analysis with respect to rent control laws. A rent control scheme must guarantee efficient landlords/lessors a just and reasonable rate of return on their investments. *Pennell v. City of San Jose*, 485 U.S. 1, 13, 108 S.Ct. 849, 858, 99 L.Ed.2d 1 (1988); *Cromwell Assocs. v. Newark*, 511 A.2d 1273, 1275 (N.J.Super.Ct.Law Div.1985) (rejecting any percentage limitation on a landlord's ability to seek rent increases under a landlord hardship provision). In addition to the just and reasonable rate of return requirement, rent control legislation must substantially advance legitimate public interests. *Richardson I*, 759 F.Supp. at 1493 (citing *Agins v. City of Tiburon*, 447 U.S. 255, 260, 100 S.Ct. 2138, 2141, 65 L.Ed.2d 106 (1980)).

b) Individualized Consideration

As indicated above, this court set forth four reasons in *Richardson I* why the approach of Ordinance 90-95, Ordinance 91-96's predecessor, did not substantially

advance the purpose of the law. One of the stated problems with Ordinance 90-95 was that "the Ordinance [did] not take into consideration the individual characteristics or market value of any piece of property in determining the maximum allowable renegotiated rent." *Richardson I*, 759 F.Supp. at 1494-96. In drafting Ordinance 91-96, the City failed to adequately address this significant defect.

The requirement of individualized consideration is apparent from other cases which have addressed taking issues. For example, in *Midkiff*, the United States Supreme Court upheld the State of Hawaii's Land Reform Act of 1967. Yet the Land Reform Act allowed the parties affected by the condemnation to present evidence of the fair market value of the subject property. *Midkiff*, 467 U.S. at 234 & n. 2, 104 S.Ct. at 2326 & n. 2 (citing Haw. Rev.Stat. § 516-56); *see also Richardson I*, 759 F.Supp. at 1494-96.

With respect to taking challenges to rent control laws, courts have recognized:

> The very nature of rent control requires that a limit be, placed on rent increases. Such limits have been held valid providing a safety valve, such as a hardship mechanism, exists which can assure, an efficient landlord a fair return. . . . [E]very rent control ordinance must be deemed to intend, and will be so read, to permit property owners to apply to the local administrative agency for relief on the ground that the regulation entitles the owner to a just and reasonable return."

Cromwell Assocs. v. Newark, 511 A.2d 1273, 1275 (N.J.Super.Ct.Law Div.1985) (citing and quoting *Hutton*

Park Gardens v. West Orange Town Council, 68 N.J. 543, 350 A.2d 1 (1975)).

Recent cases which have upheld rent control laws have involved statutes which provided for some degree of individualized consideration. For instance, under the rent control scheme in *Pennell v. City of San Jose*, 485 U.S. 1, 108 S.Ct. 849, 99 L.Ed.2d 1 (1988), when a tenant objected to a landlord's proposed rent increase, a hearing officer would determine the reasonableness of the proposed increase. *Id.* at 5, 108 S.Ct. at 853. The rent control ordinance required that the hearing officer examine "the history of the premises, the landlord's costs, and the market for comparable housing." *Id.* at 13, 108 S.Ct. at 858. The ordinance also allowed the landlord to present any other relevant financial evidence pertaining to the property. *Id.*

Moreover, even rent control schemes which have been declared unconstitutional have typically contained some mechanism for individualized consideration. *See, e.g., Birkenfeld v. City of Berkeley*, 17 Cal.3d 129, 130 Cal. Rptr. 465, 493, 550 P.2d 1001, 1029 (1976) (landlords may petition rent control board for a rent adjustment); *Cromwell Assocs.*, 511 A.2d at 1274 (rent control ordinance permitted board-approved increases in cases where the proofs demonstrate that a particular hardship forecloses on a landlord's ability to obtain a fair rate of return defined by the ordinance as an 11.5% return on investment).

In *Yee v. Escondido*, ___ U.S. ___, 112 S.Ct. 1522, 118 L.Ed.2d 153 (1992), the mobile home rent control ordinance in question prohibited rent increases without the

approval of the city council. *Id.* 112 S.Ct. at 1527. However, mobile home park owners were allowed to apply for a rent increase at any time. *Id.* The city council was required to approve any increases which it deemed "just, fair, and reasonable" after considering a nonexclusive list of eleven factors most of which pertained to the individual mobile home pads at issue. *Id.*

In contrast to the aforementioned cases, absolutely nothing in Ordinance 91-96's regulatory scheme accounts for the many unique factors, such as the rate of development in surrounding areas, which may affect the value of an individual parcel of real property at the time of renegotiation. At the hearing, the City conceded this fact.[11] To reiterate, the maximum annual renegotiated lease rent under the provisions of Ordinance 91-96 is determined solely on the basis of the *initial lease rent* and the *rent factor derived from the CPI.* The problem of lack of individual consideration in determining the renegotiated lease rent is compounded by the absence of any mechanism,

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[11] The City argued that individual considerations are accounted for in the setting of the initial lease rent at the time the lease is originated. While this may be true, the individual characteristics of a piece of property often are significantly different at the time of renegotiation than they were at the initial date of the lease which could be several decades earlier. This court need only call attention to the massive redevelopment presently underway in the Kakaako area and the planned substantial redevelopment of the Honolulu waterfront. Both of these redevelopment projects are within the City and County of Honolulu and will without question have a marked effect on property values in condominiums within, abutting, or in the vicinity of these areas.

such as a variance, for obtaining relief for special circumstances. *See Cromwell Assocs. v. Newark,* 511 A.2d 1273.4 1275 (N.J.Super.Ct.Law Div. 1985) (discussing the need for a safety valve or hardship mechanism with respect to rent control laws).

Ordinance 91-96's lack of individualized consideration is further exacerbated by the notable absence of any meaningful review process. *See Birkenfeld v. City of Berkeley,* 17 Cal.3d 129, 130 Cal.Rptr. 465, 550 P.2d 1001 (1976). In *Birkenfeld,* the California Supreme Court recognized that even when a rent control ordinance provides adequate standards for determining rental rates, the ordinance must provide procedural safeguards against unfairness in situations where the statutorily-determined rate would be unfair. *Id.* 130 Cal.Rptr. at 493-97, 550 P.2d at 1029-32.

The arbitration and appeal process in Ordinance 91-96 is focused exclusively on determining the correct initial lease rent and the rent factor from which the maximum annual renegotiated lease rent is calculated. The ordinance does *not* permit the arbitrator or the Department of Housing and Community Development to consider any other factors. At the hearing on these motions, the City conceded that the arbitration and appeal procedures are restricted to solely determining whether the maximum annual renegotiated lease rent is calculated properly under the statutory formula.

A review of the arbitration and appeal mechanism of Ordinance 91-96 reveals its inadequacies. If the lessor and lessee are unable to agree on an renegotiated lease rent, the parties must proceed to arbitration. Ord. 91-96

§ 1.4(b). In arbitration, however, the arbitrator is restricted to determining the maximum renegotiated lease rent pursuant to the ordinance's formula of initial lease rent multiplied by the rent factor. *Id.* § 1.5. The arbitrator has no authority or discretion to consider any other factors in determining the maximum renegotiated lease rent. Furthermore, while all renegotiated lease rents must be certified by the City Department of Housing and Community Development, the Department's role is similarly restricted to merely ensuring compliance with the statutory formula for determining maximum renegotiated lease rent. *Id.* § 1.9.[12]

The City contends that lessors are ensured a fair rate of return by Ordinance 91-96's two types of adjustments: (1) the biennial adjustment for inflation (§ 1.6); and the administrative adjustment for increased operating expenses (§ 1.7). The court finds that neither of these adjustments provides the type of relief which is constitutionally mandated.

The biennial adjustment allows the previously determined maximum renegotiated lease rent to increase in

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[12] In addition, any party aggrieved by the Department's action or inaction may appeal to the Department under the contested case procedures of chapter 91 of the Hawaii Revised Statutes. Ord. 91-96 § 1.9(e). Nonetheless, on appeal, there is no evidence to suggest that the Department has the authority to provide any form of relief other than ensuring compliance with Ordinance 91-96's rent formula. Furthermore, this appeal process may be nullified if a court rules, or the State attorney general or the City corporation counsel opines, that the right to appeal to the Department conflicts with chapter 658 of the Hawaii Revised Statutes.

accordance with the average consumer price index. Ord. 91-96 § 1.6. However, if the maximum renegotiated lease rent is originally set at a confiscatory rate, the biennial adjustment provides no relief from that confiscatory rate.[13] In other words, if the renegotiated lease rent is originally set at a confiscatory rate, the biennial adjustment merely prevents that confiscatory rate from becoming even more confiscatory by attempting to adjust the rate for inflation.

With respect to the administrative adjustment, that provision only applies if the lessor pays the operating expenses for the condominium exclusively from the lease rent proceeds. Ord. 91-96 § 1.7(c)(2), (d)(3). However, the uncontradicted evidence before the court indicates that lessors "almost never assume the obligation to pay a condominium project's operating expenses, and if such an obligation is assumed, the expenses are not paid exclusively from lease rent proceeds, but are paid through separate charges." Aff. of Paul J. Cathcart ¶ 3 (attached to Bishop Estate Mot. Partial Summ. J. filed 2/14/92). Thus, the court finds that the administrative adjustment provision is largely irrelevant.

Accordingly, the court finds that Ordinance 91-96 violates the Fifth Amendment's Takings Clause because it

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[13] Additionally, the court notes that the lessor is not automatically entitled to the biennial adjustment; the Department must approve such an adjustment. Ord. 91-96 § 1.6(a). As Ordinance 91-96 contains no standards for the Department to apply in determining whether to grant a biennial adjustment, the Department apparently has unlimited discretion to either grant or deny a biennial adjustment.

does not provide for consideration of individual factors which may affect the value of a particular parcel of real property at the time of renegotiation. Furthermore, Ordinance 91-96 is infirm because it does not account for situations in which the renegotiated lease rent formula does not provide the lessor with a fair rate of return. In other words, there is no meaningful mechanism for obtaining relief when the lease rent formula results in a confiscatory rate.

c) Ground Lease Premium

In addition to Ordinance 91-96's lack of individualized consideration, Bishop Estate also argues that the ordinance fails to substantially advance its public purpose because it allows a lessee to monetize a below-market rate renegotiated lease rent at the expense of the lessor. Pursuant to Ordinance 91-96, if an owner-occupant transfers his leasehold interest in a residential condominium unit to another person intending to be an owner-occupant, the renegotiated lease rent is assigned and applicable to the new owner-occupant.[14] Ord. 91-96 § 1.10. Bishop Estate contends that this provision allows an owner-occupant with a below-market rate renegotiated lease rent to sell his condominium and receive a monetary premium for the below-market rate lease rent.

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[14] The court notes that the renegotiated lease rent is not assignable if an owner-occupant transfers his leasehold interest to a new owner who does not intend to be an owner-occupant. Ord. 91-96 § 1.13. Nonetheless, this fact does not alleviate the problems associated with assignments to new owners who do intend to be owner-occupants.

In the mobile home rent control cases discussed above, the various ordinances all contained provisions which allowed tenants to transfer their rights to below-market rental rates to other buyers. *See Yee v. Escondido*, U.S. ___, 112 S.Ct. 1522, 1528-30, 118 L.Ed.2d 153 (1992); *Azul Pacifico, Inc. v. City of Los Angeles*, 948 F.2d 575, 581-82 (9th Cir.1991), *opinion withdrawn on other grounds*, 973 F.2d 704 (9th Cir.1992); *Pinewood Estates v. Barnegat Township Leveling Bd.*, 898 F.2d 347 (3d Cir.1990); *Hall v. City of Santa Barbara*, 833 F.2d 1270, 1278-80 (9th Cir.1986), *cert. denied*, 485 ___ U.S. 940, 108 S.Ct. 1120, 99 L.Ed.2d 281 (1988). The courts in those cases uniformly recognized the constitutional concerns inherent in such schemes.

The problem with rent control plans which permit the tenant to transfer his right to below-market rates is the tenant's ability to command a premium for his right. *See generally*, Werner Z. Hirsch & Joel G. Hirsch, *Legal-Economic Analysis of Rent Controls in a Mobile Home Context: Placement Values and Vacancy Decontrol*, 35 UCLA L.Rev. 399 (1988). In the mobile home cases, the premium represented the right to occupy the mobile home pad at a below-market rate. In the present case, the premium would represent the lessee's right to a below-market rate renegotiated ground lease rent. Thus, the right to receive the premium between the rent-controlled rate and the market rate is transferred from the landlord/ lessor to the tenant/lessee; this interest is worth the capitalized value of the difference between market rent and the controlled rent.

In *Hall*, the Ninth Circuit recognized the numerous Supreme Court cases which have upheld rent control

laws. 833 F.2d at 1278, nn. 19-20. The court commented, however, that none of the cases upholding rent control involved a situation in which the tenant could transfer his right to below-market rental rate to others in order to reap a monetary windfall. *Id.* The court emphasized:

> This is not a minor difference; it is crucial. The fact that the tenant can sell his interest to third parties drastically affects the economic realities of the landlord/tenant relationship. The typical rent control statute modifies the landlord/tenant relationship somewhat to protect tenants from perceived evils of the free-enterprise system.
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> That tenants normally cannot sell their rights in rent controlled property provides important safeguards for landlords. . . . If [tenants] are denied the right to cash out, tenants can enjoy the benefits of rent control only so long as they remain tenants, not beyond. When the premises become vacant, the landlord is able to reassert a measure of control over the property.

Id. at 1279.

The Third Circuit also adopted the reasoning of *Hall* in *Pinewood Estates.* In the spring of 1992, the Supreme Court commented on the premium issue in *Yee v. Escondido,* ___ U.S. ___, 112 S.Ct. 1522, 118 L.Ed.2d 153 (1992).[15] The Supreme Court in *Yee* indicated that while the rent control premium issue was not relevant to a physical

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[15] As mentioned in the physical taking discussion above, the Supreme Court in *Yee* rejected the notion set forth in *Hall* and *Pinewood Estates* that the mobile home rent control laws effected a physical taking. 112 S.Ct. at 1528-31.

taking argument, the factor was likely relevant with respect to a regulatory taking analysis.[16] ___ U.S. at ___, ___, 112 S.Ct. at 1528, 1530. In particular the court explained:

> [The mobile home park owners] are correct in citing the existence of this premium as a difference between the alleged effect of the Escondido ordinance and that of an ordinary apartment rent control statute. Most apartment tenants do not sell anything to their successors (and are often prohibited from charging "key money"), so a typical rent control statute will transfer wealth from the landlord to the incumbent tenant and all future tenants. By contrast, [the mobile home park owners] contend that the Escondido ordinance transfers wealth only to the incumbent mobile home owner. This effect might have some bearing on whether the ordinance causes a regulatory taking, it may shed some light on whether there is a sufficient nexus between the effect of the ordinance and objectives it is supposed to advance. . . . But it has nothing to do with whether the ordinance causes physical taking.

112 S.Ct. at 1530 (bold added).

In the present case, the court finds that the principles relating to "premiums" in the mobile home context are applicable to the condominium market.[17] Like mobile

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[16] The Court declined to fully address the regulatory taking claim because that issue was not included in the question on which certiorari was granted. 112 S.Ct. at 1531-34.

[17] While Ordinance 91-96 has not yet been in operation, the court notes that the "premium" argument is ripe because this

home park tenants, owner-occupants of leasehold condominiums own their housing unit, the condominium itself, but lease the underlying land. Moreover, the below-market rate lease rent which applies to the mobile home tenants and leasehold condominium owner-occupants is transferable to subsequent purchaser of the mobile home pad or condominium. With respect to both mobile homes and condominiums, the availability of a below-market rate lease rent necessarily increases the value of the subject housing unit, thereby allowing a seller to command a premium upon the sale of the housing unit. This transfer of wealth problem is generally not a concern in the area of apartment rent control because apartment rentals do not involve the ownership component present in mobile homes or condominiums.[18]

The court finds that Ordinance 91-96 enables an owner-occupant to charge a premium, in connection with the sale of a leasehold condominium with a below-market rate renegotiated lease rent, thereby operating to transfer

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case involves a facial challenge to the ordinance. In *Yee*, the Supreme Court held that an analogous facial challenge was ripe. 112 S.Ct. at 1532.

[18] The Hirschs elaborate:

> If a rent control ordinance [pertaining to apartments] allowed alienation of a tenant's rights and benefits under rent control, presumably apartment tenants could gain a benefit similar to the placement value given to mobile home park tenants. A "key money" (money spent to obtain a rent controlled apartment, usually illegally) feature to apartment rent controls might give the tenant a similar ability to monetize the benefits of rent control.

Hirsch & Hirsch, *supra*, at 425 n. 87.

value from the lessor to the lessee/seller. In light of the reasoning of the aforementioned mobile home park cases, and the analogous effects of the mobile home park laws regarding rent control and Ordinance 91-96, the court finds that the availability of the premium and the resulting transfer of wealth from the lessor to the lessee under Ordinance 91-96 violates the Taking Clause.[19]

VI. ORDINANCE 91-95

A. BACKGROUND

Ordinance 91-95 involves a mechanism for the transfer of the fee simple interest of leasehold property from condominium lessors to condominium lessees in Honolulu. In the "Findings and Purpose" section of Ordinance 91-95, the City found that there are approximately 16,000-17,000 residential condominium, cooperative and planned development units on leased land on Oahu.[20] Ord. 91-95 § 1. The City further found that the owners of such leased land had generally refused to sell proportionate shares in the land underlying such units. *Id.* As a

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[19] As the court finds Ordinance 91-96 to be unconstitutional under the Taking Clause, it need not address Bishop Estate's due process (Counts III and IV), equal protection (Count V), contracts clause (Count VI), or state law claims (Counts X and XII) claims regarding Ordinance 91-96.

[20] For the sake of simplicity, the court will refer to all condominium apartments, cooperative housing units, and planned development units covered by Ordinance 91-95 as "condominiums," unless otherwise indicated. While the court recognizes the legal distinctions between these forms of apartment ownership, such distinctions are not relevant to the issues at hand.

result of this practice, the City determined that there exists "a serious shortage of fee simple residential condominium land, cooperative housing unit land and planned development land and [ ] an artificial inflation of the value of such land on Oahu." *Id.*

Accordingly, the City concluded that owners of condominiums on leased land should be able to acquire the proportionate share of leased land underlying their units at a fair and reasonable price. *Id.* In order to accomplish this objective, the City decided to use its eminent domain power to condemn the fee simple title to the land underlying condominiums, pay just compensation to the lessors/owners of such land, and sell the land to the condominium owners. *Id.*

The City Department of Housing and Community Development ("Department") is charged with administering, enacting appropriate rules, and enforcing Ordinance 91-95. Ord. 91-95 §§ 1.7, 1.8. Article 2 of Ordinance 91-95 governs the condemnation of condominium development leaseholds.[21] The condemnation procedures are triggered once at least twenty-five of the condominium owners within the development or the owners of 50% of the condominium units, whichever is less, apply to the Department to purchase the leased fee interest. *Id.* § 2.2(a)(1). After such an application, the Department must publish notice and hold a public hearing to determine whether the acquisition of the leased fee interest

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[21] Articles 3 and 4 contain similar provisions relating to cooperative housing development leaseholds and residential planned development leaseholds, respectively.

will effectuate the public purposes of the ordinance. *Id.* at § 2.2(a)(2).

Within twelve months after the Department has designated a condominium development, or portion thereof, for acquisition, the Department must institute eminent domain proceedings unless the parties voluntarily agree to a sale of the property. Ord. 91-95 § 5.2. The compensation to be paid for the acquired property shall be the fair market value of the leased fee interest determined as of the date of the summons of the complaint in the eminent domain proceeding. *Id.* at 5.3.

After the City has acquired the subject land, authorized condominium lessees must purchase the underlying land within sixty days of acquisition. *Id.* § 2.3. In order to be eligible to buy the leased land, a purchaser must satisfy a list of seven requirements. *Id.* § 2.4.

B. TAKINGS CLAUSE (COUNT VII)[22]

1. Hawaii Housing Authority v. Midkiff

As Ordinance 91-95 involves leasehold conversion via eminent domain, the court notes that this general issue has been thoroughly addressed by the Supreme Court in a very similar case, *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 104 S.Ct. 2321, 81 L.Ed.2d 186 (1984). In that case, the plaintiffs challenged the State of

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[22] The court notes that much of the, law regarding the Takings Clause has been discussed above with respect to Ordinance 91-96. Accordingly, the court will not repeat the general discussion of Takings Clause law.

Hawaii's Land Reform Act of 1967 which created a mechanism for condemning residential lots occupied by single-family homes on which the underlying land was leased, and transferring ownership of, the condemned fees simple to the lessees. As Ordinance 91-95 is modeled after the Land Reform Act, many of the procedural aspects of the Land Reform Act are similar, if not identical, to the provisions of Ordinance 91-95 as explained.[23]

The Supreme Court in *Midkiff* rejected the plaintiffs' arguments that the Land Reform Act violated the "public use" requirement of the Fifth Amendment's Takings

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[23] The Supreme Court explained the method of condemnation under the Land Reform Act as follows:

> Under the Act's condemnation scheme, tenants living on single-family residential lots within developmental tracts at least five acres in size are entitled to ask the [HHA] to condemn the property on which they live. When 25 eligible tenants, or tenants on half the lots in the tract, whichever is less, file appropriate applications, the Act authorizes HHA to hold a public hearing to determine whether the acquisition by the State of all or part of the tract will "effectuate the public purposes" of the Act. If HHA finds that these public purposes will be served, it is authorized to designate some or all of the lots in the tract for acquisition. It then acquires, at prices set either by condemnation trial or by negotiation between lessors and lessees, the former fee owners' full "right, title, and interest" in the land.
>
> After compensation has been set, HHA may sell the land titles to tenants who have applied for fee simple ownership.

467 U.S. at 233-34, 104 S.Ct. at 2325-26 (citations and footnotes omitted).

Clause. The Court explained that its role in reviewing the legislature's judgment regarding public use is extremely narrow. 467 U.S. at 240, 104 S.Ct. at 2329 (citing *Berman v. Parker*, 348 U.S. 26, 32, 75 S.Ct. 98, 102, 99 L.Ed. 27 (1954)). The Court indicated that it would defer to the legislature's public use determination unless the use involves an "impossibility" or is "palpably without reasonable foundation." *Id.* 467 U.S. at 240-41, 104 S.Ct. at 2329-30. The Court further noted that "where the exercise of the eminent domain power is rationally related to a conceivable public purpose, the Court has never held a compensated taking to be proscribed by the Public Use Clause." *Id.* at 241, 104 S.Ct. at 2329.

Accordingly, the Supreme Court upheld the Land Reform Act. The Court recognized that the Hawaii Legislature had determined that a land oligopoly existed and that such concentration was the cause of several types of local problems. *Id.* at 241-42, 104 S.Ct. at 2329-30. The Court reasoned that regulation of an "oligopoly and the evils associated with it is a classic exercise of a State's police powers." *Id.* at 242, 104 S.Ct. at 2330.

The Court further found that the Land Reform Act's approach to correcting the land oligopoly problem was not irrational. *Id.* The Court elaborated:

> [The Land Reform Act,] like any other, may not be successful in achieving its intended goals. But "whether *in fact* the provision will accomplish its objectives is not the question: the [constitutional requirement] is satisfied if . . . the . . . [state] Legislature *rationally could have*

> *believed* that the [Act] would promote its objective." When the legislature's purpose is legitimate and its means are not irrational, our cases make clear that empirical debates over the wisdom of takings no less than debates over the wisdom of other kinds of socio-economic legislation are not to be carried out in the federal courts. Redistribution of fees simple to correct deficiencies in the market determined by the state legislature to be attributable to land oligopoly is a rational exercise of the eminent domain power. Therefore, the Hawaii statute must pass the scrutiny of the Public Use Clause.

467 U.S. at 242-43, 104 S.Ct. at 2330.

2. The Present Case

In light of the Supreme Court's holding and reasoning in *Midkiff* as well as the similarity between the Land Reform Act and Ordinance 91-95, the court finds little merit to Bishop Estate's taking argument regarding Ordinance 91-95. Bishop Estate argues that the public purpose of Ordinance 91-95 is without reasonable foundation. In particular, Bishop Estate maintains that the ordinance is based on the incorrect assumption that a concentration of land ownership currently exists with respect to land leased for condominiums which is similar to the oligopoly which justified the Land Reform Act in the single-family home context. Bishop Estate contends that there is no concentration of land ownership in relation to leased land underlying condominium projects.

The court finds no merit to this argument. The Supreme Court in *Midkiff* repeatedly emphasized the substantial deference which should be accorded to the relevant legislative body in the area of public use. 467 U.S. at 239-43, 104 S.Ct. at 2328-31. In the present case, the City Council determined that ownership of land beneath residential condominium projects is concentrated in the hands of owners who have refused to sell proportionate shares in their fee simple titles to lessees residing in the condominium units. Ord. 91-95 § 1. Thus, the City Council's primary concern was apparently the inability of the owners of leasehold condominiums to purchase proportionate shares of the underlying fee simple title. While the current concentration of land ownership with respect to leasehold condominiums may not be as drastic as the land oligopoly which prompted the Land Reform Act,[24] this contention does not undermine the City's determination that permitting leasehold condominium owners to purchase the underlying property serves a legitimate public purpose.

Bishop Estate also argues that Ordinance 91-95 fails to provide lessors with just compensation. It claims that they are entitled to severance damages for the partial condemnation of their leased land. It also contends that

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[24] Nonetheless, the court notes that Bishop Estate's own filings reveal that in 1987 the land underlying 45% of the condominium projects in Hawaii was owned by only 51 lessors. Bishop Estate Mot. Summ. J. filed 2/14/92, Ex. CC, at ii. Furthermore, at the time Ordinance 91-95 was enacted, Bishop Estate alone owned the fee simple interest under approximately 12,500 of the leasehold condominium units. Bishop Estate Mem. Opp. filed 6/29/92, at 8.

Ordinance 91-95 fails to exclude the effects that Ordinance 91-96 has on the valuation of the leased fees.

Bishop Estate's argument regarding just compensation is untenable. As section 5.3 of Ordinance 91-95 provides for payment of compensation equivalent to "the current fair market value of the leased fee interest," the ordinance clearly comports with the constitutional requirements for just compensation. *See United States v. Reynolds*, 397 U.S. 14, 16, 90 S.Ct. 803, 805, 25 L.Ed.2d 12 (1970).[25] Any arguments as to the proper manner of calculating current fair market value and the appropriate factors to be considered are premature in this facial challenge at this point in time.[26] *Southern Pacific v. City* of *Los*

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[25] In *Reynolds*, the Supreme Court explained:

> And "just compensation" means the full monetary equivalent of the property taken. The owner is to be put in the same position monetarily as he would have occupied if his property had not been taken. In enforcing the constitutional mandate, the Court at an early date adopted the concept of market value: *the owner is entitled to the fair market value of the property at the time of the taking.*

397 U.S. at 16, 90 S.Ct. at 805 (footnotes omitted) (emphasis added).

[26] The court notes that Bishop Estate's argument regarding just compensation is distinct from the reasonable rate of return inquiry associated with Ordinance 91-96. With respect to Ordinance 91-96, the court had to determine whether a taking existed. One of the factors in determining whether a taking has occurred is whether the landowner will still be able to receive a fair rate of return on his property. In contrast, as Ordinance 91-95 involves complete condemnation, it necessarily involves a taking. Thus, the pertinent question is whether the landowner receives "just compensation" for the taking.

Angeles, 922 F.2d 498, 505-07 (9th Cir.1990) (facial takings challenge alleging denial of just compensation is not ripe unless the plaintiff has sought compensation through the available procedures), *cert. denied*, ___ U.S. ___, 112 S.Ct. 382, 116 L.Ed.2d 333 (1991); *see also Richardson I*, 759 F.Supp. at 1481. The City Department of Housing and Community Development has yet to enact the necessary rules to effectuate Ordinance 91-95. More importantly, the state courts have not had an opportunity to interpret and apply the compensation provisions of Ordinance 91-95. In sum, Ordinance 91-95 states that landowners shall be paid fair market value; accordingly, in the absence of evidence to the contrary, this court assumes that all factors necessary to comply with constitutional requirements will be considered.[27]

C. SUBSTANTIVE DUE PROCESS (COUNT VIII)

In order to prevail on its substantive due process claim, Bishop Estate must establish that Ordinance 91-95 is "arbitrary and irrational." *Del Monte Dunes v. City of Monterey*, 920 F.2d 1496, 1508 (9th Cir.1990). Bishop Estate claims that Ordinance 91-95 does not have a legitimate government purpose and that the ordinance is not rationally related to the alleged legislative purpose. The court finds no merit to Bishop Estate's substantive due process claim.

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[27] The Ninth Circuit has held that a determination of "fair market value" may include severance damages. *United States v. 50.50 Acres of Land*, 931 F.2d 1349, 1358 (9th Cir.1991); see *generally Georgia-Pacific Corp. v. United States*, 226 Ct.Cl. 95, 640 F.2d 328 (1980).

This court rejected these same type of arguments with respect to Bishop Estate's taking claim discussed above. The court further notes that a plaintiff has an extraordinarily high burden to carry in order to demonstrate that a legislative enactment is arbitrary and irrational under the due process clause. *See Del Monte Dunes*, 920 F.2d at 1508. Moreover, courts should give substantial deference to a legislature's determination of a public use or purpose as well as the legislative means for carrying out the purpose. *Midkiff*, 467 U.S. at 239-243, 104 S.Ct. at 2328-31. In *Midkiff*, the Supreme Court specifically recognized that the use of the government's eminent domain power to effect lease-to-fee conversion is a rational response to serious housing problems. *Id.* at 242-43, 104 S.Ct. at 2330-31. The Court in *Midkiff* stated that it found no merit to the plaintiffs' due process claim and it disposed of the matter in two sentences in a footnote. *Id.* at 243 n. 6, 104 S.Ct. at 2330 n. 6.

D. Equal Protection (Count IX)

Generally, equal protection challenges are evaluated under rational-basis scrutiny to see whether the legislation at issue is irrational or wholly arbitrary. *Conti v. City of Fremont*, 919 F.2d 1385, 1389 (9th Cir.1990). Classifications based upon race, however, are presumptively invalid. *Personnel Adm'r of Mass. v. Feeney*, 442 U.S. 256, 272, 99 S.Ct, 2282, 2292, 60 L.Ed.2d 870 (1979). Nonetheless, the Supreme Court has made clear that "even if a neutral law has a disproportionately adverse effect upon a racial minority, it is unconstitutional under the Equal Protection Clause only if that impact can be traced to a discriminatory purpose." *Feeney*, 442 U.S. at 272, 99 S.Ct.

at 2292 (emphasis added) (citing *Washington v. Davis*, 426 U.S. 229, 96 S.Ct. 2040, 48 L.Ed.2d 597 (1976), and *Arlington Heights v. Metropolitan Housing Dev. Corp.*, 429 U.S. 252, 97 S.Ct. 555, 50 L.Ed.2d 450 (1977)).

Thus, if the official action in question is race-neutral on its face, a plaintiff asserting an equal protection claim based upon race must prove the existence of racially discriminatory intent or purpose in order to prevail. *Arlington Heights*, 429 U.S. at 265, 97 S.Ct. at 563. The Supreme Court has cautioned that discriminatory intent or purpose requires more than simply intent as volition or awareness of consequences. *Feeney*, 442 U.S. at 279, 99 S.Ct. at 2296. A plaintiff must demonstrate that the legislation at issue was enacted "at least in part 'because of,' not merely 'in spite of,' its adverse effects upon an identifiable [racial] group." *Id.*; *see also Stop H-3 Ass'n v. Dole*, 870 F.2d 1419, 1431-32 (9th Cir.1989).

For the purposes of the present case, a brief examination of *Feeney* is instructive. In that case, female plaintiffs challenged a Massachusetts statute which gave veterans a preference for state civil service jobs. The plaintiffs alleged that the law violated their rights under the Fourteenth Amendment's Equal Protection Clause because the statute operated overwhelmingly to the advantage of men since over 98% of veterans were male.

Initially, the Supreme Court noted that the statute was gender-neutral on its face as it distinguished only between veterans and non-veterans, not men and women. 442 U.S. at 274, 99 S.Ct. at 2293. The Court reasoned that the law could not be rationally explained on the basis of gender:

> Veteran status is not uniquely male. Although few women benefit from the preference the non-veteran class is not substantially all female. To the contrary, significant numbers of non-veterans-male as well as female-are placed at a disadvantage. Too many men are affected by [the veterans preference law], to permit the inference that the statute is but a pretext for preferring men over women.

Id. at 275, 99 S.Ct. at 2294. In addition, the court noted that the statute's unfortunate impact upon women was easily explained, in a gender-neutral manner by the legislature's completely legitimate goal of aiding veterans. *Id.*

Furthermore, the Supreme Court in *Feeney* rejected the plaintiffs' allegations of gender-based discriminatory purpose. 442 U.S. at 276-80, 99 S.Ct. at 2294-97. Asserting that a person intends the natural and foreseeable consequences of his voluntary actions, the plaintiffs argued that the Massachusetts legislature must have intended to discriminate against women because the statute foreseeably and inevitably operated to the great disadvantage of women. *Id.* at 278, 99 S.Ct. at 2295. While the Court recognized the statute's foreseeable adverse consequences to women, the Court emphasized that there was no evidence that the preference for veterans was devised to harm women. *Id.* at 279, 99 S.Ct. at 2296. In essence, the purpose of the statute was clearly to help veterans, not to discriminate against women. *Id.* at 279-80, 99 S.Ct. at 2296-97.

In the present case, Bishop Estate argues that Ordinance 91-95 intentionally discriminates against Native

Hawaiians. It contends that the discrimination is demonstrated in part by the fact that Bishop Estate and Liliuokalani Trust, two of the top five landowners affected by Ordinance 91-95, were created specifically for the benefit of Native Hawaiians.[28] Bishop Estate Mem.Opp. filed 6/29/92, at 7. However, Bishop Estate's equal protection arguments exhibit the same type of flaws as that of the plaintiffs' claims in *Feeney*.

Ordinance 91-95 is undoubtedly racially neutral on its face. Ordinance 91-95 applies to residential leasehold condominium lessors and lessees irrespective of the race or ethnic background of the affected parties. The impact of the ordinance is shared by all lessors, many of which, if not the majority, are not Native Hawaiian. Analogous to *Feeney*, too many non-Native Hawaiian lease fee owners are affected by Ordinance 91-95 to permit the inference that the statute is but a pretext for preferring non-Native Hawaiians over Native Hawaiians.

The present case is also similar to *Feeney* in that the plaintiffs have failed to establish any discriminatory intent or purpose. Like the legislators in *Feeney*, the drafters of Ordinance 91-95 were likely aware of the effect that the ordinance would have on entities, such as Bishop Estate, which are connected with Native Hawaiian

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[28] More specifically, Bishop Estate argues that the alleged discriminatory purpose of Ordinance 91-95 against Native Hawaiians is evidenced by: disproportionate impact, history of public land policy, erroneous findings of fact, procedural irregularities in enacting the ordinance, the City's knowledge of the ordinance's impact, and the official action taken to enact the ordinance. Bishop Estate Mem.Opp. filed 6/29/92, at 5-30.

ethnicity. However, in this case as well as *Feeney*, a perfectly legitimate government purpose explains the impetus of the legislation. Whereas *Feeney* involved aid to veterans, Ordinance 91-95 was enacted in response to the critical problems in the Honolulu housing market, in particular leasehold condominiums. Thus, the court finds that the City has a legitimate public purpose for enacting Ordinance 91-95 and there is no credible evidence to support the notion that Ordinance 91-95 is but a pretext for discriminating against Native Hawaiians.

E. STATE CONSTITUTIONAL CLAIMS (COUNT XI)

In Count XI, Bishop Estate claims that Ordinance 91-95 violates its rights under the takings, due process, and equal protection clauses of the Hawaii State Constitution. While the Hawaii State Constitution is generally modeled after the United States Constitution, the scope of its protections are not necessarily the same. *Hawaii Housing Authority v. Lyman*, 68 Haw. 55, 704 P.2d 888, 896 (1985). However, the legal analysis of Bishop Estate's claims under the aforementioned state constitutional provisions is essentially the same as the inquiry under the corresponding sections of the United States Constitution.[29] *See, e.g. id.* 704 P.2d at 897 (takings clause); *State v. Cotton*, 55 Haw. 148, 516 P.2d 715, 719 (1973) (due process clause); *Estate of Coates v. Pacific Eng'g*, 71 Haw. 358, 791

[29] Moreover, the court notes that all of the parties have relied on the same arguments to support their positions on the state constitutional claims as they did with respect to the federal constitutional claims.

P.2d 1257, 1260 (1990) (equal protection clause). Accordingly, for the same reasons that this court rejected Bishop Estate's federal constitutional claims above, the court similarly finds its state constitutional arguments unpersuasive.

F. State Statutory Claims (Count XIII)

In Count XIII, Bishop Estate contends that Ordinance 91-95 is preempted by various Hawaii state statutes. In particular, it claims that Ordinance 91-95 is preempted by the comprehensive provisions set forth in Hawaii Revised Statutes chapters 101 (eminent domain), 516 (residential leasehold condominiums and cooperatives), 519 (real property leases), 514A (condominiums), and 421H (cooperative housing corporations). For the reasons set forth below, the court certifies the preemption question to the Hawaii Supreme Court.[30]

The United States Supreme Court has consistently approved of the use of certified questions to state supreme courts when a federal court case involves an important question of state law which is both unclear under state legal precedent and would be determinative in the instant case. *Virginia v. American Booksellers Ass'n*, 484 U.S. 383, 393-98, 108 S.Ct. 636, 643-46, 98 L.Ed.2d 782

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[30] The court need not certify the state law questions regarding Bishop Estate's claims under the Hawaii State Constitution because there is sufficient state law to enable this court to make an informed decision on these issues. Moreover, Rule 13(a) of the Hawaii Rules of Appellate Procedure permits certification only when there is no controlling precedent in the Hawaii judicial decisions.

(1988); *Bellotti v. Baird*, 428 U.S. 132, 150-52, 96 S.Ct. 2857, 2867-68, 49 L.Ed.2d 844 (1976); *Lehman Bros. v. Schein*, 416 U.S. 386, 389-92, 94 S.Ct. 1741, 1743-45, 40 L.Ed.2d 215 (1974); *Clay v. Sun Ins. Office*, 363 U.S. 207, 212, 80 S.Ct. 1222, 1225, 4 L.Ed.2d 1170 (1960).[31] In *Lehman*, the Supreme Court explained:

> [Use of state certification procedures] does, of course, in the long run save time, energy, and resources and helps build a cooperative judicial federalism. Its use in a given case rests in the sound discretion of the federal court.

416 U.S. at 391, 94 S.Ct. at 1744 (footnote omitted).

While federal courts should not abdicate their duty to decide issues properly before them by routinely certifying questions to state supreme courts, certification under appropriate circumstances can result in significant conservation of the litigants' time and money as well as judicial resources. The Ninth Circuit Court of Appeals has not hesitated to certify questions to state supreme courts when such questions involved important issues of unsettled state law which were controlling in the federal case.[32] District courts have similarly utilized the certification process. *See, e.g., Burdick v. Takushi*, 737 F.Supp. 582

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[31] Most of the aforementioned cases as well as the succeeding cases regarding certification have extensive subsequent cases histories in light of the certified questions. As these cases are mentioned only as examples of certification and not for their substantive holdings, the court will omit the subsequent case histories

[32] *See, e.g., Alaska Airlines v. United Airlines*, 902 F.2d 1400, 1403-05 (9th Cir.1990); *Morrell Constr. v. Home Ins. Co.*, 899 F.2d 875 (9th Cir.1990); *Kunz v. Utah Power & Light Co.*, 871 F.2d 85, 87-88 (9th Cir.1989); *Torres v. Goodyear Tire & Rubber Co.*, 867 F.2d

(D.Haw.1990) (on remand following Ninth Circuit's reversal, district court certified three questions with respect to Hawaii election laws and write-in votes). The decision whether to certify a state law question to the state supreme court rests in the sound discretion of the federal district court. *Louie v. United States*, 776 F.2d 819, 824 (9th Cir.1985).

In order for a federal court to be able to certify a question to a state supreme court, the state court must provide a specific procedure for receiving such questions. The Hawaii Supreme Court has authorized certified questions in Rule 13 of the Hawaii Rules of Appellate Procedure. Pursuant to Rule 13(a), a federal district court may certify a question to the Hawaii Supreme Court when such question (1) concerns Hawaii law which is (2) determinative of the cause and (3) there is no clear controlling precedent in the Hawaii judicial decisions.

In the present case, the court finds that Count XIII involves issues of state law which are determinative of the validity of Ordinance 91-95. The court further finds that the there is no clear controlling precedent in the Hawaii judicial decisions which disposes of these state law issues. In particular, this court finds conflicting authority as to whether Hawaii Revised Statutes chapter 101, which governs eminent domain procedures, preempts Ordinance 91-95.

1234, 1237-39 (9th Cir.1989); *Toner for Toner v. Lederle Labs.*, 779 F.2d 1429, 1432-34 (9th Cir.1986); *Aetna Ins. Co. v. Craftwall of Idaho*, 757 F.2d 1030, 1034 (9th Cir.1985); *Meckert v. Transamerica Ins. Co.*, 742 F.2d 505, 506-07 (9th Cir.1984).

On the other hand, the Hawaii legislature enacted the Land Reform Act which has eminent domain procedures nearly identical to those of Ordinance 91-95. Thus, the Hawaii legislature has specifically authorized certain types of eminent domain procedures which conflict with the general provisions of chapter 101. Furthermore, the State Attorney General has opined that Ordinance 91-95 is not preempted by state law.[33] On the other hand, relevant Hawaii statutory law seems to indicate that the City must utilize the eminent domain procedures in chapter 101 which appear to conflict with the procedures in Ordinance 91-95.

In addition the preemptory issues raised here implicate a broader question regarding the various county's authority to enact legislation in areas occupied, or at least partially occupied, by state law. While the Supreme Court of Hawaii has in the past addressed this question, as this case illustrates there remains significant room for interpretation and thus confusion. This question is of significant importance to both the counties and the state and transcends the boundaries of this case. Because this involves a pure question of state law and policy, in the final analysis it must be decided by the Hawaii Supreme Court.

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[33] *See* Opinion of the Attorney General of the State of Hawaii dated October 4, 1991, at 1. (Bishop Estate Mot. Partial Summ.J. filed 2/14/92, Ex. R). Nonetheless, the Attorney General did not specifically address the issue of preemption relating to chapter 101. To the contrary, the Attorney General seemed to indicate that the City must utilize its eminent domain power pursuant to the procedures provided in chapter 101. *Id.* at 2.

This court is fully aware of the fact that certification in this case will cause some initial delay while the Hawaii Supreme Court addresses the certified question. Nonetheless, if this court were not to certify the state law preemption question, the court is confident that the Ninth Circuit Court of Appeals would itself order such certification in light of the controlling nature of the important, unsettled state law and policy issues. The court notes that the Ninth Circuit Court of Appeals has often certified questions to the Hawaii Supreme Court.[34]

Leaving the certification to the court of appeals would only cause further delay as well as undue confusion and uncertainty in the interim while the parties consider whether to act upon this court's decision on these purely state law issues in light of the pending appeal. Therefore, while certification will result in some initial delay, it will obviate a much greater delay and substantial confusion in the likely event the Ninth Circuit

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[34] *See, e.g., Smith v. Cutter Biological,* 911 F.2d 374 (9th Cir. 1990) (Ninth Circuit certified three questions regarding the Hawaii Blood Shield Law); *Graulty v. Bank of Hawaii,* 856 F.2d 78 (9th Cir.1988) (Ninth Circuit certified question pertaining to Hawaii Uniform Fiduciaries Act); *In re Asbestos Cases,* 829 F.2d 907 (9th Cir.1987) (Ninth Circuit certified question relating to Hawaii products liability law); *United States v. Allstate Ins. Co.,* 825 F.2d 243 (9th Cir.1987) (Ninth Circuit certified question regarding the government's ability to recover medical care costs under Hawaii law) ; *Kinoshita v. Canadian Pacific Airlines,* 803 F.2d 471 (9th Cir.1986) (Ninth Circuit certified question of Hawaii contract law) ; *Robinson v. Ariyoshi,* 753 F.2d 1468 (9th Cir.1985) (Ninth Circuit certified six questions regarding Hawaii water law issues).

were to certify the preemption question while the case was on appeal.

Upon careful review of the relevant state law and the underlying state policy implications involved, the court finds that the purely state law preemption issue would be best answered in the first instance by the Hawaii Supreme Court. Accordingly, the court will certify this question to the Hawaii Supreme Court under Rule 13 of the Hawaii Rules of Appellate Procedure, and retain jurisdiction pending a determination by the Hawaii Supreme Court.

CONCLUSION

In *Richardson I*, this court held that Ordinance 91-96's predecessor statute, Ordinance 90-95, was unconstitutional for a number of reasons. Subsequent to that decision, the City, in enacting Ordinance 91-96, made an attempt to remedy the problems with Ordinance 90-95. While the City managed to correct some of the constitutional infirmities of Ordinance 90-95, it failed to appropriately address other defects. For the reasons stated above, the court GRANTS Bishop Estate's motion for partial summary judgment with respect to Ordinance 91-96 finding the ordinance unconstitutional for the reasons stated herein and DENIES the City's and the HALE Coalition's motions for partial summary Judgment regarding Ordinance 91-96.

With respect to Ordinance 91-95, this court has found the ordinance to be in compliance with the relevant provisions and standards of the United States Constitution and the Constitution of the State of Hawaii. Therefore,

the court GRANTS the City's and HALE Coalition's motions for partial summary judgment with respect to the federal and state constitutional claims pertaining to Ordinance 91-95 finding the ordinance in compliance with federal and state constitutional standards and DENIES Bishop Estate's motion for partial summary judgment on those same claims.

The court also CERTIFIES to the Supreme Court of Hawaii the following question:

> According to Hawaii state law, is Ordinance 91-95 preempted by Hawaii Revised Statutes chapters 101, 516, 516D, 519, 514A, or 42 1 H?

The parties are ordered to submit the appropriate certificate in accordance with this court's separate order regarding certification.

IT IS SO ORDERED.

APPENDIX C

UNITED STATES DISTRICT COURT
D. HAWAII

Civ. No. 92-00372 HMF
SMALL LANDOWNERS OF OAHU,
a Hawaii nonprofit corporation,
Plaintiff,

V.

CITY AND COUNTY OF HONOLULU,
a Hawaii municipal corporation,
Defendant.

Sept. 16, 1993

ORDER GRANTING DEFENDANT'S MOTION FOR SUMMARY JUDGMENT

FONG, District Judge.

INTRODUCTION

On August 30, 1993, the court heard oral argument on cross motions for summary judgment filed by Plaintiff Small Landowners of Oahu ("Small Landowners") and Defendant City and County of Honolulu (the "City").

The subject of this lawsuit is the constitutionality of Ordinance 91-95, a condominium lease-to-fee ordinance similar to the single family residence lease-to-fee statute upheld by the United States Supreme Court in *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 104 S.Ct. 2321, 81 L.Ed.2d 186 (1984).

In a case brought by the Bishop Estate, Judge David Ezra of this court had previously held that Ordinance 91-95 was constitutional under both the United States and Hawaii constitutions. *Richardson, et al., v. City and County of Honolulu (Richardson II)*, 802 F.Supp. 326 ___ (D.Haw. 1992), Exh. A to the City's Motion. Before a ruling on the *summary* judgment motions, Small Landowners unsuccessfully attempted to intervene in that case. *Richardson II*, Order of July 6, 1992, Exh. C to City's Motion.

BACKGROUND

Ordinance 91-95 was enacted on December 8, 1991.

In *Richardson II*, the court explained the operation of Ordinance 91-95 as follows:

> Ordinance 91-95 involves a mechanism for the transfer of the fee simple interest of leasehold property from condominium lessors to condominium lessees in Honolulu. In the "Findings and Purpose" section of Ordinance 91-95, the City found that there are approximately 16,000-17,000 residential condominium, cooperative and planned development units on leased land on Oahu.[1] Ord. 91-95 § 1. The City further found that the owners of such leased land had generally refused to sell proportionate shares in

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[1] For the sake of simplicity, the court will refer to all condominium apartments, cooperative housing units, and planned development units covered by Ordinance 91-95 as "condominiums," unless otherwise indicated. While the court recognizes the legal distinctions between these forms of apartment ownership, such distinctions are not relevant to the issues at hand.

the land underlying such units. *Id.* As a result of this practice, the City determined that there exists "a serious shortage of fee simple residential condominium land, cooperative housing unit land and Planned development land and [ ] an artificial inflation of the value of such land on Oahu." *Id.*

Accordingly, the City concluded that owners of condominiums on leased land should be able to acquire the proportionate share of leased land underlying their units at a fair and reasonable price. *Id.* In order to accomplish this objective, the City decided to use its eminent domain power to condemn the fee simple title to the land underlying condominiums, pay just compensation to the lessors/owners of such land, and sell the land to the condominium owners. *Id.*

The City Department of Housing and Community Development ("Department") is charged with administering, enacting appropriate rules, and enforcing Ordinance 91-95. Ord. 91-95 §§ 1.7, 1.8. Article 2 of Ordinance 91-95 governs the condemnation of condominium development leaseholds.[2] The condemnation procedures are triggered once at least twenty-five of the condominium owners within the development or the owners of 50% of the condominium units, whichever is less, apply to the Department to purchase the leased fee interest. *Id.* § 2.2 (a)(1). After such an application, the Department must publish notice and hold a public hearing to

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[2] Articles 3 and 4 contain similar provisions relating to cooperative housing development leaseholds and residential planned development leaseholds, respectively.

> determine whether the acquisition of the leased fee interest will effectuate the public purposes of the ordinance. *Id.* § 2.2 (a)(2).
>
> Within twelve months after the Department has designated a condominium development, or portion thereof, for acquisition, the Department must institute eminent domain proceedings unless the parties voluntarily agree to a sale of the property. Ord. 91-95 § 5.2. The compensation to be paid for the acquired property shall be the fair market value of the leased fee interest determined as of the date of the summons of the complaint in the eminent domain proceeding. *Id.* § 5.3.
>
> After the City has acquired the subject land, authorized condominium lessees must purchase the underlying land within sixty days of acquisition. *Id.* § 2.3. In order to be eligible to buy the leased land, a purchaser must satisfy a list of seven requirements. *Id.* § 2.4.

Richardson II Summary Judgment Order at 29-32, City's Exh. C.

SUMMARY JUDGMENT STANDARD

Rule 56(c) of the Federal Rules of Civil Procedure provides that summary judgment shall be entered when:

> . . . the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

The moving party has the initial burden of "identifying for the court those portions of the materials on file that it believes demonstrate the absence of any genuine issue of material fact." *T.W. Elec. Serv., Inc. v. Pacific Elec. Contractors Ass'n*, 809 F.2d 626, 630 (9th Cir.1987) (citing *Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 106 S.Ct. 2548P 2553, 91 L.Ed.2d 265 (1986)). The movant need not advance affidavits or similar materials to negate the existence of an issue on which the opposing party will bear the burden of proof at trial. *Celotex*, 477 U.S. at 323, 106 S.Ct. at 2553.

If the moving party meets its burden, then the opposing party must come forward with "specific facts showing that there is a genuine issue for trial" in order to defeat the motion. Fed.R.Civ.P. 56(e); *T.W. Elec.*, 809 F.2d at 630. The opposing party cannot stand on the pleadings nor simply assert that it will discredit the movant's evidence at trial. *Id.* "If the factual context makes the [opposing] party's claim *implausible*, that party must come forward with more persuasive evidence than would otherwise be necessary to show that there is a genuine issue for trial." *Cal. Arch. Bldg. Prods. v. Franciscan Ceramics*, 818 F.2d 1466, 1468 (9th Cir.1987) (citing *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 587, 106 S.Ct. 1348, 1356, 89 L.Ed.2d 538 (1986)).

The standard for summary judgment reflects the standard governing a directed verdict. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 250, 106 S.Ct. 2505, 2512, 91 L.Ed.2d 202 (1986)). When there is a genuine issue of material fact, "the judge must assume the truth of the evidence set forth by the [opposing] party with respect to that fact." *T.W. Elec.*, 809 F.2d at 631. Inferences from the

facts must be drawn in the light most favorable to the non-moving party. *Id.*

DISCUSSION

I. PRECLUSIVE EFFECT OF RICHARDSON II

The City argues that the decision in *Richardson II* precludes Small Landowners from relitigating the constitutionality of Ordinance 91-95. The City advances res judicata (claim preclusion), collateral estoppel (issue preclusion), and judicial estoppel as the sources of the preclusion.

Res judicata or claim preclusion provides that a final judgment, "when rendered on the merits, is an absolute bar to a subsequent action between the same parties or those in privity with them, upon the same claim or demand." *IB Moore's Federal Practice* ¶ 0.405[1] at p. III-4.

The City concedes that Small Landowners was not a party to the earlier suit, but argues that Small Landowners was in privity with the plaintiffs in *Richardson II*. "Privity" is more a conclusion based on the individual facts than a rigorous test. 18 Charles A. Wright, Arthur R. Miller, & Edward H. Cooper, *Federal Practice and Procedure* § 4449 (1981). The predominant factor in determining privity is the connection between the two parties. *Id.* While both the *Richardson II* plaintiffs and Small Landowners are owners of condominiums affected by the statute, there is no other link shown. Thus, they are not in privity. Res judicata does not preclude Small Landowners.

The City argues in the alternative that collateral estoppel or issue preclusion bars relitigation of the issues decided in *Richardson II*. The doctrine of nonmutual collateral estoppel sometimes gives preclusive effect to earlier judgments obtained in litigation against others. *See Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation*, 402 U.S. 313, 91 S.Ct. 1434, 28 L.Ed.2d 788 (1971); *Green v. Ancora-Citronelle Corp.*, 577 F.2d 1380, 1384 & n. 2 (9th Cir.1978). The most important limitation on nonmutual preclusion is that the party precluded had a "full and fair opportunity to litigate in the prior action." 18 Charles A. Wright, Arthur R. Miller, & Edward H. Cooper, *Federal Practice and Procedure* § 4465 (1981).

Small Landowners did not have a full and fair opportunity to litigate in *Richardson II*. It would be unfair to bind them to a result that they were denied an opportunity to influence through their own arguments. Furthermore, if the City wanted to bind Small Landowners by the decision in *Richardson II*, it could have and should have joined Small Landowners as a party to that litigation. *Martin v. Wilks*, 490 U.S. 755, 109 S.Ct. 2180, 104 L.Ed.2d 835 (1989). Thus, Small Landowners is not collaterally estopped by *Richardson II*.

Finally, the City argues that principles of "judicial estoppel" preclude Small Landowners from relitigating the constitutionality of Ordinance 91-95.

Judicial estoppel does not apply here. The doctrine of judicial estoppel prevents a party from asserting a position that is inconsistent with an earlier position taken in the litigation. *Yanez v. United States*, 989 F.2d 323 (9th

Cir.1993). Here, Small Landowners has not asserted any inconsistent earlier positions.

II. CONSTITUTIONAL CHALLENGES TO ORDINANCE 91-95

Both sides have moved for summary judgment on Small Landowners' claims that Ordinance 91-95 effects an impermissible taking, that it violates substantive due process, and that it violates the Equal Protection Clause.

A. Takings Clause (Count I, VII, XIV)

Count VII of the complaint alleges that Ordinance 91-95 effects an impermissible taking in violation of the Fifth Amendment to the United States Constitution. Count XIV alleges a violation of the Takings Clause of the Hawaii State Constitution. Count I alleges that the taking was a deprivation of constitutional rights actionable under 42 U.S.C. § 1983.

The Takings Clause of the Fifth Amendment to the United States Constitution states that "private property [shall not] be taken for public use, without just compensation." The Takings Clause applies to the states through the Fourteenth Amendment. *Hawaii Housing Authority v. Midkiff*, 467 U.S. 229, 244 n. 7, 104 S.Ct. 2321, 2331 n. 7, 81 L.Ed.2d 186 (1984). Moreover, a state may delegate its power to condemn to a municipality. *Cf. Jacobson v. Tahoe Regional Planning Agency*, 566 F.2d 1353 (9th Cir.1977), *aff'd in part and rev'd in part on other grounds*, 440 U.S. 391, 99 S.Ct. 1171, 59 L.Ed.2d 401 (1979).

In *Midkiff*, the United States Supreme Court upheld Hawaii's Land Reform Act of 1967. That statute provided for condemnation of the fee simple interest of the land under leasehold single family residences. The Hawaii legislature had passed the Land Reform Act in an effort to correct a land oligopoly.

The Supreme Court found that the Land Reform Act's approach to correcting the land oligopoly problem was not irrational. *Id.* The Court elaborated:

> [The Land Reform Act,] like any other, may not be successful in achieving its intended goals. But "whether *in fact* the provision will accomplish its objectives is not the question: the [constitutional requirement] is satisfied if . . . the . . . [state] Legislature *rationally could have believed* that the [Act] would promote its objective." When the legislature's purpose is legitimate and its means are not irrational, our cases make clear that empirical debates over the wisdom of takings, no less than debates over the wisdom of other kinds of socioeconomic legislation are not to be carried out in the federal courts. Redistribution of fees simple to correct deficiencies in the market determined by the state legislature to be attributable to land oligopoly is a rational exercise of the eminent domain power. Therefore, the Hawaii statute must pass the scrutiny of the Public Use Clause.

467 U.S. at 242-43, 104 S.Ct. at 2330.

The Takings Clause analysis under the Hawaii Constitution is similar. Article I, section 20 of the Hawaii Constitution reads, "private property shall not be taken or damaged for public use without just compensation." In

Hawaii Housing Authority v. Lyman, 68 Haw. 55, 704 P.2d 888 (1985), the Hawaii Supreme Court adopted a very deferential position similar to that in *Midkiff:*

> We therefore hold that once the legislature has spoken on the social issue involved, so long as the exercise of the eminent domain power is rationally related to the objective sought, the legislative public use declaration should be upheld unless it is palpably without reasonable foundation. The crucial inquiry is whether the legislature might reasonably consider the use public, and whether it rationally could have believed that application of the sovereign's condemnation powers would accomplish the public use goal.

Id. at 70-71, 704 P.2d 888.

The court now turns to the specific arguments advanced by Small Landowners.

1. The City Council's Findings

Small Landowners first argues that the City Council's findings are unsupported by the record. Specifically, Small Landowners asserts that there is no oligopoly in condominium ownership, that there is no shortage of fee simple condominiums, and that many lessees are financially better off than lessors.

Small Landowners has a difficult burden in attacking the City Council's findings of fact. The court must give deference to a legislative body's factual findings. A party challenging a factual finding made by a legislative body must show that "the legislative facts [relied upon] could

not reasonably be conceived to be true by the governmental decisionmaker." *Vance v. Bradley*, 440 U.S. 93, 110-11, 99 S.Ct. 939, 949-50, 59 L.Ed.2d 171 (1979); *Lamb v. Scripps College*, 627 F.2d 1015 (9th Cir.1980).

Small Landowners suggests that the court should not defer to the factual findings of the City Council because it is a municipality rather than a state legislature. Although Small Landowners correctly notes that municipalities and states are treated differently in the Eleventh Amendment immunity context, Small Landowners does not cite any case authority supporting its suggested distinction in this area.

The distinction is unwarranted because the deference given to legislative findings reflects a concern with the separation of powers between the legislature and the judiciary. It is as offensive to disturb the findings of city legislators as it is to disturb the findings of state legislators.

Moreover, despite the law review articles cited by Small Landowners, property owners are not "discrete and insular minorities" who deserve special judicial protection because they lack access to the political system. *United States v. Carolene Products Co.*, 304 U.S. 144, 58 S.Ct. 778, 82 L.Ed 1234 (1938). The absurdity of this suggestion is shown by the fact that the Bishop Estate is one of the institutions challenging this statute. The power of the Bishop Estate in Hawaii belies any claim that it lacks access to the political system.

Small Landowners suggests that the Supreme Court's decision in *Lucas v. South Carolina Coastal Council* signals reduced deference to legislative findings. ___ U.S. ___, 112

S.Ct. 2886, 120 L.Ed.2d 798 (1992). The *Lucas* Court rejected the South Carolina legislature's finding that construction on plaintiff's beach front property could be curtailed because it threatened serious public harm. In order to avoid compensating plaintiff for a regulatory taking, the Court held, the legislature would need to find that common law principles such as nuisance allowed the prohibition of the construction. *Id.* ___ U.S. at ___, ___, 112 S.Ct. at 2901-02.

Lucas does not mean that all legislative findings are suspect. Rather, it is distinguishable because the South Carolina legislature had a vested interest in finding that the plaintiff's use of his property caused harm. If the legislature determined that the use was harmful, it could restrict that use without paying compensation to the plaintiff. Thus, the legislature's finding of harm was inherently suspect. There is no reason to extend this heightened scrutiny to physical Takings cases in which the legislature has already committed itself to paying compensation.

Thus, the court will give great deference to the City Council's findings. The City Council need not consider the best evidence. Rather, it must simply have some evidence that could convince a rational legislator of the truth of the findings.

Applying this standard, the court finds adequate support for the City Council's findings.[3] For example, the

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[3] The court does not need to examine every finding. The findings that are supported provide an adequate basis for the Council to have passed the ordinance.

City Council found that the leasehold condominium system allowed lessors to renegotiate large lease rent increases. This is supported by the statements of many persons who testified before the City Council.[4] Similarly, the testimony supported the City Council's findings that some lessees could not buy the fee simple interest without a mandatory conversion program,[5] and that lessees were forced to surrender their improvements on the land.[6]

Small Landowners most vigorously attacks the City Council's finding that land ownership is concentrated in the hands of owners who have refused to sell their fee simple interests. Citing statistics, Small Landowners argues that the fee simple interests are spread among many owners and that there is no concentration of ownership.[7] Thus, Small Landowners contends, there is no oligopoly that would support the passage of the ordinance as in *Midkiff*.

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[4] *See, e.g.*, statements of Theresa Miyamoto, CX00019; Helen Higgins, ("I live at the Sandalwood, the apartment that was raised from affordable living to unaffordable right now.") CX00020; Darvin Haupert (lease rent increased by 8000 percent), CX00026-27; Knud Lindgard, CS00220; Richard Rosen, CX00252. All numbers refer to Bate stamp numbers given in Small Landowners' Exhibit 1.

[5] *See* Small Landowners Exhibit 1, testimony of Steve Holmes, CX00251; Edward Jurkens, CX00285; Jerome Manis, CX00283.

[6] *See*, Small Landowners Exhibit 1, Knud Lindgard, CX00220; Darvin Haupert, CX00215.

[7] *See* Ezra, O'Connor, Moon & Tam Report, Exhibit 4 to Small Landowners' Motion, at 47 (415 of 466 landowners (89%) own land under only one condominium project).

Small Landowners' argument is fruitless. First, the City Council's finding is not that there is an oligopoly, but rather that ownership is concentrated among landowners who have refused to sell. That finding almost proves itself because landowners who have agreed to sell are no longer owners. Moreover, the fact that landowners have refused to sell is supported by the statements cited above. Thus, the City Council's finding has adequate support.

Second, even if the finding was unsupported, it would not invalidate the ordinance. The City Council made several adequately supported findings upon which it could rationally decide to exercise its eminent domain power. Small Landowners has not succeeded in invalidating those findings.

2. The Use of Mandatory Conversion

Small Landowners argues that even if the findings are accepted, the mandatory conversion is irrational because it cannot correct these problems. Small Landowners supports its argument by noting that single-family residence prices rose after the mandatory conversion program went into effect. Thus, Small Landowners suggests, a rational legislator could not believe that condominium prices would fall.

The City Council's choice need not be a wise one, it must merely be rational. Ordinance 91-95 passes this minimal test. Transferring the fee simple title to the lessees will end the problem of gouging lessees on lease rent negotiations. The ordinance will force sales by unwilling lessors. Furthermore, it will allow lessees to keep the

value of their improvements on the land. The means chosen by the City Council is a rational one.

3. Public Use Without Public Funds

Small Landowners further argues that there is no taking "for public use" because private funds are used in the conversion.

This argument was flatly rejected in *Midkiff*. There, the Supreme Court upheld the legislature's finding of public use despite the fact that private funds were used to buy the fee simple interests. *Midkiff*, 467 U.S. at 241, 104 S.Ct. at 2329. The question is not the source of the funds, but rather whether the legislature rationally believed that the taking served a public purpose. *Id.*

The City Council reasonably believed that its eminent domain could solve the numerous problems that it found to have been caused by the condominium lease system. Thus, its decision to exercise its power comports with the constitution.

4. Taking of a Cotenancy

Small Landowners argues that the City may not condemn only a portion of the land, leaving the building's owner in a forced cotenancy with the former lessees. Small Landowners cites the following sentence from *Hendler v. United States*, 952 F.2d 1364, 1374 (Fed.Cir.1991): "The Government does not have the right to declare itself a co-tenant-in-possession with a property owner."

The citation is taken completely out of context, and does not affect the result here. In *Hendler*, the district

court had held that no taking occurred when the statute allowed EPA inspectors to enter the land and conduct monitoring. The appellate court reversed, holding that the government's entry onto land was a taking of the right to sole possession, and was therefore compensable. *Id.* at 1374. The *Hendler* court did not hold, as Small Landowners suggests, that the government can never take a portion of a property and leave the rest. The government's ability to take only a limited interest in property has been repeatedly affirmed. *See, e.g., Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982) (government must pay for taking of land necessary for a roof top cable).

5. Inadequate Compensation

Small Landowners asserts that Ordinance 91-95 under-compensates the present owners for the value of the taken fee simple interests. This claim is unripe because the procedures challenged have never been used. *Southern Pacific v. City of Los Angeles*, 922 F.2d 498, 505-07 (9th Cir. 1990) (facial takings challenge alleging denial of just compensation is not ripe unless the plaintiff has sought compensation through the available procedures), *cert. denied*, ___ U.S. ___, 112 S.Ct. 382, 116 L.Ed.2d 333 (1991).

6. Generalized Claims of Unfairness

Small Landowners makes several generalized claims of unfairness as well.

Small Landowners argues that the City's tax policies forced landowners to develop condominiums which will be taken away by Ordinance 91-95. Even if this seems harsh to the landowners, it is not a basis to invalidate Ordinance 91-95. Tax policy can create social problems that a city may attempt to solve by rational means. Ordinance 91-95 is a rational attempt to solve the ills that the City Council found, whatever their source.

Small Landowners notes that all five of the City Council members who voted for Ordinance 91-95 have interests in leasehold condominiums. This is not a basis to invalidate the statute. If it were, the City Council could never pass any statute dealing with condominiums. Disclosure of their interests allows the public to correct any problem through the political process.

B. SUBSTANTIVE DUE PROCESS (COUNTS VIII AND XV)

Counts VIII and XV allege that Ordinance 91-95 violates Small Landowners' substantive due process rights under the Fourteenth Amendment to the United States Constitution and Article 1, section 5 of the Hawaii Constitution.

In order to prevail on these claims, Small Landowners must establish that Ordinance 91-95 is "arbitrary and irrational." *Del Monte Dunes v. City of Monterey*, 920 F.2d 1496, 1508 (9th Cir.1990); *State v. Cotton*, 55 Haw. 148, 153, 516 P.2d 715 (1973). As explained above, Small Landowners does not meet this burden because the ordinance is a rational exercise of legislative power.

C. EQUAL PROTECTION (COUNTS IX, XVI)

Counts IX and XVI allege that Ordinance 91-95 violates Small Landowners' equal protection rights guaranteed by the Fourteenth Amendment to the United States Constitution and Article 1, section 5 of the Hawaii Constitution. Small Landowners argues the ordinance irrationally groups small landowners with owners such as Bishop Estate who own many projects.

Legislative classifications not involving a suspect class must be rationally related to furthering a legitimate state interest. *Massachusetts Board of Retirement v. Murgia*, 427 U.S. 307, 312, 96 S.Ct. 2562, 2566, 49 L.Ed.2d 520 (1976); *Estate of Coates v. Pacific Engineering*, 71 Haw. 358, 363, 791 P.2d 1257 (1990). Here, the City Council found that the refusal of both large and small landowners to sell their land created economic problems. Thus, the City Council rationally decided to treat the problem by subjecting both large and small landowners to mandatory conversion. There is no constitutional problem with this approach.

Small Landowners misplaces two other arguments under the equal protection banner. First, it asserts that Ordinance 91-95 violates equal protection because landowners who are forced to sell their properties will have a difficult time avoiding taxes by replacing them with tax free "like kind" properties. This is definitely a disadvantage to those forced to sell, but it is not an equal protection violation.

Second, Small Landowners again asserts the unfairness of forcing land owners into a cotenancy with their former lessees. Again, this does not show the use of an

irrational classification, so it is not a violation of the Equal Protection Clause.

In summary, the court holds that Ordinance 91-95 is constitutional under both the federal and state constitutions. Accordingly, the court DENIES Small Landowners' motion for summary judgment, and GRANTS the City's motion for summary judgment on Counts I, VII, VIII, IX, XIV, XV, and XVI of the complaint.

III. COMPLIANCE WITH THE CITY CHARTER (COUNT XXII)

The City moves for summary judgment on Count XXII which alleges that Ordinance 91-95 conflicts with procedural requirements of Section 3-110 of the City Charter. Section 3-110 requires that the City Council, prior to taking property under its eminent domain power, shall adopt a resolution declaring the necessity of the taking as well as other information regarding the property.

This issue is not ripe for a facial challenge to the statute. When the City actually condemns property, it will presumably be required to comply with the Charter. That question should be reserved for another day. Accordingly, the court GRANTS the City's motion for summary judgment on Count XXII.

CONCLUSION

In summary, this case is indistinguishable from *Midkiff*, and the lenient standards set there compel a

conclusion that Ordinance 91-95 is a rational and constitutionally permissible exercise of the eminent domain power.

IT IS SO ORDERED.

APPENDIX D

ORDINANCE NO. 91-96 BILL NO. 36 (1991)
CD-2, FD-1

A BILL FOR AN ORDINANCE RELATING TO LEASE RENT.

BE IT ORDAINED by the People of the City and County of Honolulu:

SECTION 1. Findings and Purpose.

The council finds that:

(1) According to the State of Hawaii Data Book 1990 by the Department of Business and Economic Development, the City and County of Honolulu had within its jurisdiction in 1987:

(A) A total of 25,203 condominium housing units which were owner-occupied; and

(B) Of that total, 16,291 or approximately sixty-five percent were on leased land;

(2) No information has been presented to the council suggesting that the data under paragraph (1) has changed appreciably since 1987;

(3) Testimony has been presented to the council that owner-occupants of condominium apartments were not informed of the terms and conditions of lease rent renegotiation provisions of their leases. Additionally, the terms and conditions of the lease, including the rent and renegotiation provisions, did not result from negotiations between lessors and individual owner-occupants, but instead were established unilaterally by the lessors. Accordingly, it is reasonable to presume that the lessor

was acting in its own best interest and established the lease rent according to the then prevailing market lease rents;

(4) From and after 1990, the lease rents for a substantial portion of the condominium housing units on leased land are due for renegotiation;

(5) Testimony has been presented to the council that one condominium in Honolulu, the Sandalwood, has experienced lease rent increases of over 1,000 percent at the time of rent renegotiation and that similar increases will affect owner-occupants of other condominiums in the City and County. Unless controlled, the renegotiated lease rents may be unaffordable to many owner-occupants of leased condominium housing units;

(6) If renegotiated lease rents become unaffordable, the owner-occupants may have no recourse but to terminate their leases or sell their leasehold interests and seek housing elsewhere; and

(7) Residential leaseholds have had and continue to have the following undesirable economic effects:

(A) The increases in the value of land have caused lease rentals to increase on renegotiation of rentals (on the expiration of 25 to 30 years of initial fixed rent periods) to 1,000 percent, for renegotiated lease rentals are invariably tied to the fee simple value of the land on which the leasehold residential apartments are situated, and these new lease rentals have at times exceeded the amount of the payments that the lessee had been making on the leasehold mortgages;

(B) Lease rent renegotiations have strongly favored the lessor, the lessee having little option but to consent to such rental as determined by the lessor or to give up the leasehold and home, although the lease may yet have 25 or more years to run;

(C) The inequality of bargaining power has allowed lessors to charge lease rent based not only on the raw land value of the property but also on the value of the offsite and onsite improvements which have already been paid for or will be paid for by the lessee and on the value accruing thereon;

(D) The uncertainty associated with the expected high increases in lease rentals at the time of rent renegotiation have adverse economic impact on the marketability of such apartments since financing institutions are reluctant to give long-term mortgages to prospective buyers of such apartments; and

(E) Residential leaseholds have also undesirable social effects. Lease rent negotiations are usually scheduled every 10 to 15 years after the initial fixed rent period of 25 to 30 years. Thus, as the lessee advances in age and the lessee's income potential declines, the lessee's lease rentals increase, causing the lessee to give up the lease and to look for other accommodations. This situation aggravates the already acute need for government-sponsored low and middle income and elderly housing. With the increasing number of elderly in this county, the problem promises to become even more acute in the foreseeable future, and will adversely affect the health and welfare of these people and the general welfare of the people of the City and County of Honolulu.

The council further finds and declares:

(1) That the land is to be considered as a source of life, dignity, and economic freedom for the people who reside on it;

(2) That it is the policy of the City and County of Honolulu that the owner-occupant lessee of a residential apartment, so long as remaining a lessee, shall have the right to have rentals set at reasonable levels and to enjoy the owner-occupant lessee's leasehold estate under reasonable leasehold terms:

(3) That the increase in land value was not caused by the efforts of the lessors or the lessees and to allow lease rent increases to be based on the current land values would result in incredible hardship to lessees. Further, lease rent increases of 1,000 percent would make home ownership unaffordable to a substantial number of owner-occupants of residential condominiums. In view of the already tight housing market in the City and County of Honolulu, such a result would be unconscionable. Accordingly, the council believes it is equitable to reform lease rent renegotiation provisions affecting residential condominiums so that the renegotiated lease rent is affordable to owner-occupant lessees while still providing a fair return to the lessors;

(4) Section 46-1.5(20), Hawaii Revised Statutes, authorizes the City to regulate the "renting, subletting, and rental conditions of property for places of abode by ordinance," and section 46-1.5(13), Hawaii Revised Statutes, authorizes the City to "enact ordinances deemed

necessary to protect health, life, and property, and preserve the order and security of the county and its inhabitants";

(5) Pursuant to the authority of section 46-1.5(20), the council adopted Ordinance 90-95, which imposed maximum renegotiated lease rents for condominium housing and certain other units;

(6) Ordinance 90-95 was invalidated by the United States District Court of the District of Hawaii in Richardson v. City, Civil No. 90-00856;

(7) The Court invalidated the ordinance for, among other reasons, its broad application to more than "residential condominiums," which appear to mean owner-occupied condominium housing units and because the application of the rent cap formula to the "initial lease rent" (where the "initial lease rent" was the beginning lease rent) did not yield a reasonable return to the lessor;

(8) Unlike investor-owned or commercial apartments, owner-occupied condominium housing units are intended for use as homes and not for business or income producing purposes;

(9) The initial lease rent in an apartment lease reflects the reasonable market value rent for that apartment on the effective date of said lease and, accordingly, increasing the initial lease rent by the percentage change in the consumer price index for Honolulu from the effective date of the lease to the renegotiation date results in affordable lease rents to apartment owner-occupants and reasonable returns to the lessor;

(10) Consequently, the establishment of maximum renegotiated lease rents for owner-occupied condominium housing units, with the provision of fair return to lessors, serves the public purpose of maintaining the affordability of housing for owner-occupants; and

(11) That the public health, safety, and welfare of the people of the City and County of Honolulu demand that this Ordinance be fully implemented and that other applicable laws be enacted, including legislation to prevent the imposition of confiscatory economic burdens upon the thousands of lessee apartment owners presently living on leased property.

The purpose of this Ordinance is to set maximum renegotiated lease rents which are affordable to condominium apartment owner-occupants and fair to lessors. This Ordinance is intended to be in conformance with *Richardson v. City.*

SECTION 2. The Revised Ordinances of Honolulu 1978, as amended, is amended by adding a new chapter to be appropriately designated and to read as follows:

CHAPTER ___
MAXIMUM ANNUAL RENEGOTIATED LEASE RENT

Sec.___-1.1. Definitions.

For the purposes of this chapter:

"Apartment," "association of apartment owners," "condominium," "declaration of horizontal property regime," and "declaration of condominium property regime" mean the same as defined under Chapter 514A, Hawaii Revised Statutes.

"Apartment lease" means an apartment owner-occupant's lease for the owner-occupant's apartment and includes any lease to an apartment owner-occupant for the land upon which the owner-occupant's apartment is situated, including, but not limited to a ground lease and/or a condominium conveyance document.

"Apartment owner" means a person holding, or the persons jointly or in common holding, a leasehold interest in a residential apartment.

"Apartment owner-occupant" is defined in section – 1.2.

"Condominium project" means a building containing at least one residential apartment.

"Consumer price index" means the Consumer Price Index For All Urban Consumers (CPI-U) for Honolulu published by the Bureau of Labor Statistics of the United States Department of Labor.

"Declaration" means a declaration of horizontal property regime or declaration of condominium property regime.

"Department" means the department of housing and community development.

"Fixed rent period" means the period of a lease during which the lease rent for a residential apartment is stated in the lease, even if the rent is not held constant for the entire period.

"Initial lease rent" means the beginning lease rent specified in an apartment lease or the reasonable market

value rent prevailing at the effective date of the apartment lease determined as specified in section ___-1.4, whichever is greater. This term specifically excludes any lease rents that reflect reduced rent at the beginning of the lease due to construction of the project or due to special negotiations between the developer and the land owner.

"Land owner" means the person holding the leased fee interest in the land on which a condominium project is situated.

"Lease" means a lease or master lease, including any sandwich interest, affecting a residential apartment. A sandwich interest means any lease or sublease in the chain of title between the land owner's – interest in-the land and the apartment lease.

"Lease rent" means the rent payable by a lessee to a lessor for the leasehold interest for a residential apartment under an apartment lease.

"Lessee" means any person to whom land on which a condominium project is situated is leased or subleased.

"Lessor" means any person who leases or subleases land on which a condominium project is situated.

"Maximum annual renegotiated lease rent," "maximum lease rent," or "maximum" means the maximum annual renegotiated lease rent applicable to an apartment owner-occupant, as determined under section ___-1.5 or biennially adjusted under section – 1.6.

"Renegotiated lease rent" means the lease rent determined in accordance with this chapter on the renegotiation dates specified in the lease.

"Renegotiated rent period" means any period of a lease following the expiration of the fixed rent period.

"Renegotiation date" means the date on which a renegotiated lease rent is to take effect.

"Residential apartment" means a condominium apartment which is used for residential purposes. The term does not include the following:

(1) An apartment used for commercial purposes;

(2) An apartment used as a time share unit or transient vacation unit as defined under chapter 21A, article 9; or

(3) Any parking, recreational, or other nonresidential condominium apartment.

Sec.___-1.2. **Apartment Owner-Occupant Definition.**

(a) For the purpose of this chapter, an "apartment owner-occupant" or "owner-occupant" means an owner of a residential apartment who on the renegotiation date of the lease of the residential apartment occupies the residential apartment as the owner's principal residence.

(b) An apartment owner shall be deemed to occupy a residential apartment if, on the renegotiation date of the lease, the residential apartment serves as the principal place of residence of the apartment owner and the apartment owner has possessory control of the premises at that time. An apartment owner shall not be deemed to have possessory control of the premises if the residential apartment is rented, leased, or otherwise assigned to another person or entity for any period of time. Proof of residency

and possessory control shall be established by rules adopted by the department.

Sec.___-1.3. Applicability, Purpose of Chapter.

(a) This chapter:

(1) Applies to all leases that contain provisions for renegotiation of lease rents for the residential apartment of an apartment owner-occupant. This chapter shall apply whether the leases were executed prior to the effective date of this chapter or are executed from the effective date of this chapter. This chapter also shall apply to lease rent renegotiations that are concluded after the effective date of this chapter,

(2) Sets a maximum annual renegotiated lease rent for the apartment of an owner-occupant;

(3) Allows biennial adjustment of renegotiated lease rent during the renegotiated rent period;

(4) Allows the administrative adjustment of renegotiated lease rent for a residential apartment to an amount higher than the applicable maximum. Administrative adjustment is allowed when the lessor pays operating expenses for the apartment; and

(5) Establishes a process for certification that a renegotiated lease rent for the residential apartment of an apartment owner-occupant is within the maximum.

(b) This chapter does not and shall not be construed as setting a maximum lease rent or adjustment or certification process for lease rent payable during a fixed rent

period or for a residential apartment that is not owned by an owner-occupant.

Sec.___-1.4. Renegotiation Provisions.

(a) Every lease shall include or be deemed to include the following provisions:

(1) Renegotiation of lease rent shall occur no more frequently than every ten years from and after the rent renegotiation date; provided, that the first renegotiation shall not be scheduled before the fifteenth year following the initial date of the lease;

(2) After any renegotiation, the renegotiated lease rent for the residential apartment of an apartment owner-occupant shall not exceed the maximum under section – 1.5;

(3) During a renegotiated rent period, the renegotiated lease rent for a residential apartment may be further adjusted biennially in accordance with section – 1.2; and

(4) The renegotiated lease rent for a residential apartment may exceed the applicable maximum if administratively adjusted pursuant to section – 1.7.

(b) In the event the parties to an apartment lease are unable to reach agreement under any reopening provision, the department or its designee shall arbitrate, and the maximum lease rent as determined by arbitration shall be certified by the department as provided for in section ___- 1. 9; provided that where section 5 16D- 12, Hawaii Revised Statutes, is applicable, the arbitration

shall proceed pursuant to chapter 516D. Arbitration proceedings under this subsection will be subject to the following requirements:

(1) An advance deposit, which amount shall be determined by the department, equal to projected expenses and fees of the department or its designee for arbitration proceedings shall be required and shall be paid equally by lessors and lessees. All additional expenses and fees incurred by the department or its designee while acting as the arbitrator shall be borne equally by the lessees and the lessors. These additional expenses and fees shall be subject to monthly billings or other arrangements which may be specified by contract. If more than one lessee is involved in an arbitration proceeding, all lessees shall share equally in one-half of the arbitration costs. The same division of costs shall apply if more than one lessor is involved in a proceeding.

(2) Failure on the part of any lessee to comply with the provisions of this subsection, including failure to make advance deposits on payments, shall result in forfeiture of any rights or remedies under this chapter for arbitration, and the lessee's sole rights and remedies shall be as provided in the lease.

(3) If any lessor fails to comply with the provisions of this subsection, including failure to make advance deposits or payments, then arbitration proceedings under this chapter will cease and lease rent shall be set at the most recent fixed lease rent. Upon compliance with the provisions set forth herein, the arbitration may proceed, with the determination of the new lease rent effective from the date of compliance by the lessor.

Sec.___-1.5. Maximum Annual Renegotiated Lease Rent.

(a) Except as otherwise specified under this subsection, the annual renegotiated lease rent payable from any renegotiation date by an owner-occupant for a residential apartment shall not exceed the maximum annual renegotiated lease rent established in accordance with this section. Only when administratively adjusted pursuant to section ___-1.7 may the annual renegotiated lease rent exceed the maximum.

(b) The maximum annual renegotiated lease rent for a residential apartment shall be the initial lease rent multiplied by a rent factor. The rent factor shall be determined by dividing:

(1) The average consumer price index for the six-month period in which the rent renegotiation occurs; by

(2) The average consumer price index for the six-month period in effect at the time of the effective date of the initial lease rent.

(c) For purposes of determining the maximum annual renegotiated lease rent, the applicable consumer price index shall be the index in effect on the renegotiation date. The council is aware that the consumer price index is an average figure that is published every six months and may not accurately reflect the change in consumer prices as it applies to Honolulu on the renegotiation date. Accordingly, the maximum renegotiated lease rent may be adjusted within a six-month period to reflect the actual change, if any, and the adjusted amount

shall be the maximum renegotiated lease rent for that period.

Sec.___-1.6. Biennial Adjustment of Renegotiated Lease Rent.

(a) During a renegotiated rent period, the renegotiated lease rent for the residential apartment of an owner-occupant may be adjusted biennially by the lessor in accordance with this section. A lessor may, but is not required to biennially adjust the lease rent for the residential apartment. If biennially adjusting the lease rent, the lessor may do so only with the approval of the department.

A renegotiated lease rent for a residential apartment, as adjusted in accordance with this section, shall be deemed within the applicable maximum.

(b) For the purpose of this section:

"Biennially adjusted lease rent" means the annual renegotiated lease rent, as biennially adjusted.

"Current lease rent" means the annual renegotiated lease rent in effect prior to a biennial adjustment.

"Effective date of biennially adjusted lease rent" means the date on which a biennially adjusted lease rent takes effect. As provided under subsection (c) of this section, that date is two years after the effective date of the current lease rent.

(c) During a renegotiated rent period, the renegotiated lease rent for the residential apartment of an owner-occupant may be adjusted biennially. The biennially

adjusted lease rent shall be determined by multiplying the current lease rent by a rent factor. The rent factor shall be determined by dividing:

(1) The average consumer price index for the six-month period encompassing the effective date of the biennially adjusted lease rent; by

(2) The average consumer price index for the six-month period encompassing the effective date of the current lease rent.

The biennially adjusted lease rent shall be effected from the date which is two years after the effective date of the current lease rent.

(d) When there is less than two years between the effective date of the current lease rent and the commencement of a new renegotiated rent period, the current lease rent shall not be biennially adjusted under this section.

(e) The council is aware that the consumer price index is an average figure that is published every six months and may not accurately reflect the change in consumer prices as it applies to Honolulu on the biennial adjustment date. Accordingly, the biennially adjusted lease rent may be revised with a six-month period after the official reporting of the applicable consumer price index. The revision shall reflect the actual, official change, if any, in the consumer price index. The revised amount shall be the biennially adjusted lease rent in effect.

Sec.___-1.7. Administrative Adjustment of Annual Renegotiated Lease Rent To Higher Than Maximum.

(a) The annual renegotiated lease rent for the residential apartment of an owner-occupant may be adjusted by the department to an amount higher than the maximum applicable to that apartment. An administrative adjustment shall be made in accordance with this section and only for the circumstances of subsection (c) or (d).

(b) For the purpose of this section:

"Administratively adjusted lease rent" means the annual renegotiated lease rent, as administratively adjusted.

"Base year" means the last year of the fixed rent period.

"Base year act operating income" means the lessor's net operating income from the apartment during the base year. If the lessor shows that the net operating income from the apartment during the base year was lower than normal of extraordinary or unusual expenses, the department may adjust the base year net operating income to reflect an appropriate amount.

"Fair net operating income" means net operating income from the apartment, as adjusted for inflation, which is the same as the base year net operating income. Inflation shall be measured by the change in the consumer price index from the base year to the years for which the Administrative adjustment is proposed.

"Operating expenses" mean:

(1) Common expenses assumed by the lessor and unpaid by apartment owners or other lessees of the condominium project;

(2) Expenses for services provided by the lessor which primarily benefit the apartment owners of the condominium project;

(3) Expenses for maintenance by the lessor of apartments or facilities of the condominium project;

(4) Real property taxes;

(5) Special or improvement district assessments imposed:

(A) By the State or City for the funding of public projects; and

(B) On the owner of the condominium project or land on which the condominium project is situated;

(6) Expenses for telephone, electricity, gas, water, sewer, or cable television services used by apartment owners;

(7) Expenses for rehabilitation or repair of apartments or other facilities of the condominium project; and

(8) Payments of debt service incurred for the construction of onsite or offsite improvements.

(A) "Offsite improvements" mean all physical improvements:

(i) Constructed or placed off the land on which the condominium project is situated; and

(ii) Which are to be used in common by occupants of all lands adjoining the improvements or by occupants of all lands for whose benefit the improvements have been constructed or placed; and

(B) "Onsite improvements" mean all physical improvements:

(i) Constructed or placed on the land on which the condominium project is situated; and

(ii) Which are for the benefit of apartment owners and other lessees in the condominium project.

"Onsite improvements" include, but are not limited to, dwelling units, garages, stairs, walkways, driveways, walls, trees, shrubs, landscaping, and pools.

"Operating expenses for the apartment" mean operating expenses which:

(1) Are paid directly for the residential apartment; or

(2) Represent the proportionate share of the operating expenses attributable to the residential apartment, when the operating expenses are not paid directly for the apartment.

"Operating income from the apartment" means lease rent paid for the residential apartment.

"Net operating income" means operating income from the apartment less operating expenses for the apartment.

(c) The annual renegotiated lease rent for the residential apartment of an owner-occupant may be administratively adjusted to an amount higher than the maximum applicable to that apartment if:

(1) The lessor paid operating expenses for the apartment during the base year;

(2) The lessor paid those operating expenses exclusively from lease rent proceeds and not from separate charges;

(3) In the years for which the adjustment is proposed, the lessor will continue to pay those operating expenses exclusively from lease rent proceeds; and

(4) The lessor's net operating income from the apartment in the years for which the adjustment is proposed will be less than the lessor's base year net operating income.

The administratively adjusted lease rent for the residential apartment shall be set to maintain a fair net operating income to the lessor. The administratively adjusted lease rent shall be valid for as long as the lessor continues to pay the operating expenses for the residential apartment. When the lessor discontinues payment of all or a portion of the operating expenses, the administratively adjusted lease rent shall be readjusted by the lessor to reflect the discontinuation.

An administratively adjusted lease rent under this subsection may be biennially adjusted pursuant to section -1.6. The department shall establish a method of calculating the biennial adjustment to maintain the lessor's fair net operating income.

(d) The annual renegotiated lease rent for the residential apartment of an owner-occupant may be administratively adjusted to an amount higher than the maximum applicable to that apartment if:

(1) The lessor paid no operating expenses for the apartment during the last year of the fixed rent period;

(2) In the years for which the adjustment is proposed, the lessor will pay operating expenses for the apartment; and

(3) The lessor will pay those operating expenses exclusively from lease rent proceeds and not from separate charges.

The administratively adjusted lease rent for the residential apartment shall be set to allow the lessor to pass on the operating expenses to the apartment owner-occupant. The administratively adjusted lease rent shall be valid for as long as the lessor continues to pay the operating expenses for the residential apartment. When the lessor discontinues payment of all or a portion of the operating expenses, the administratively adjusted lease rent shall be readjusted by the lessor to reflect the discontinuation.

An administratively adjusted lease rent under this subsection may be biennially adjusted pursuant to section -1.6. The department shall establish a method of calculating the biennial adjustment to maintain the pass-on of the operating expenses.

(e) A lessor desiring an administrative adjustment of the annual renegotiated lease rent for a residential apartment shall petition the department. The petition

shall specify the proposed adjusted lease rent and be accompanied by supporting data.

Upon receipt of a petition, the department:

(1) Shall review the proposed adjusted lease rent and supporting data;

(2) Shall give the lessor an opportunity to be heard;

(3) May conduct its own study of the lessor's operating income and operating expenses or appraisal of the residential apartment or condominium project; and

(4) May request the lessor to provide additional data.

Within ninety days of the submission of the petition, the department shall approve, disapprove, or modify the proposed adjusted lease rent. Upon approval, disapproval, or modification, the department shall notify the lessor and owner-occupant of the residential apartment From the effective date of the adjustment, the lessor may charge the administratively adjusted lease rent for the residential apartment.

If the department disapproves a proposed adjusted lease rent for the residential apartment, the lessor shall not charge a lease rent higher than the maximum lease rent applicable to that apartment.

If the department does not take action within the ninety-day period, the proposed adjusted lease rent shall be deemed approved and effective on the ninety-first day following submission. The department shall notify the lessor and owner-occupant of the residential apartment.

(f) The department shall determine the cost incurred for each proceeding to adjust a lease rent. The lessor shall be charged for the cost incurred by the department for the proceeding; except that the lessor shall not be charged:

(1) For the cost of any study or appraisal undertaken by the department without the lessor's permission;

(2) If the department took no action on the proposed adjustment within the ninety-day period under subsection (e); or

(3) If the department waives the charge to prevent undue financial hardship on the lessor.

The department shall require the lessor to reimburse the department for the chargeable incurred costs, whether the proposed adjusted lease rent is approved, disapproved, or modified. All reimbursements received by the department shall be deposited into the general fund.

(g) The approval, disapproval, or modification of a proposed adjusted lease rent may be appealed by the lessor or apartment owner-occupant. An appeal shall be made in writing to the department within thirty days of the approval, disapproval, or modification.

An appeal shall not stay the administratively adjusted lease rent, as approved or modified by the department.

Upon the receipt of an appeal, the department shall refer the appeal to a hearing officer. The hearing officer shall:

(1) Hold an agency hearing in accordance with the contested case procedures of chapter 91, Hawaii Revised Statutes; and

(2) Issue a decision and order confirming, modifying, or disapproving the department's action.

The department may institute a civil action in any court of competent jurisdiction for the enforcement of a decision and order pursuant to this section.

Sec.___-1.8.Interest in Lease Rent Payments.

The lessor, including the master lessor and any sandwich position, shall share in the receipt or lease rentals paid by the owner-occupants and other lessees, as adjusted by this section, in accordance with their respective interests. Notwithstanding any contrary provision in any contract or lease, a developer or other person entitled to share in the lease rent payments shall share in such lease rent payments by the owner-occupants and other lessees to the extent of the developer's or other person's interest as may be determined by agreement of those entitled to share in the payment of lease rentals by owner-occupants and other lessees, or in the absence of such agreement, pursuant to chapter 658, Hawaii Revised Statutes.

Sec.___-1.9. Certification Of Renegotiated Lease Rents After Renegotiation.

(a) In the lease rent renegotiation process, the renegotiated lease rent for an apartment owner-occupant may

be set by arbitration as provided in section -1.4(b) or by voluntary agreement without arbitration.

(b) Each renegotiated lease rent set by an arbitrator or by voluntary agreement without arbitration shall not exceed the applicable maximum.

(c) After being set by an arbitrator or voluntary agreement, but prior to taking effect, each renegotiated lease rent shall be submitted to the department. The purpose of the submission to the department is for certification that the renegotiated lease rent is within the applicable maximum. The apartment owner-occupant and lessor shall jointly submit the renegotiated lease rent. Upon submission, the department:

(1) May hold an agency hearing on the renegotiated lease rent;

(2) May require the apartment owner-occupant and lessor to submit relevant information; and

(3) May conduct its own study and investigation.

(d) The renegotiated lease rent shall be deemed within the maximum if:

(1) The department so certifies within thirty days of the submission of the renegotiated lease rent; or

(2) The department fails to issue a certification by the thirtieth day following the submission of the renegotiated lease rent.

If, within thirty days of submission, the department certifies that the renegotiated lease rent is not within the

maximum, the renegotiated lease rent shall be invalid and shall not take effect. The department shall order the apartment owner-occupant and lessor to renegotiate again.

(e) A party aggrieved by the department's action or inaction under this section may appeal to the department. Upon receipt of an appeal, the department shall:

(1) Hold an agency hearing in accordance with the contested case procedures of chapter 91, Hawaii Revised Statutes; and

(2) Issue an appropriate decision and order.

(f) If a court of competent jurisdiction rules or the state attorney general or corporation counsel opines that an renegotiated lease rent set by an arbitrator may be vacated, modified, or corrected only pursuant to chapter 658, Hawaii Revised Statutes, and not by action of the department, an action to vacate, modify, or correct the renegotiated lease rent set by an arbitrator shall be subject to chapter 658, Hawaii Revised Statutes, and no appeal of the renegotiated lease rent set by an arbitrator shall be made to the department.

Sec. ___-1.10. Assignment of Renegotiated Lease Rent To Another Apartment Owner-Occupant.

If, during a renegotiated rent period, an apartment owner-occupant conveys or transfers the leasehold interest in a residential apartment to another person intending to be an owner-occupant, the renegotiated lease rent for

the residential apartment shall be assigned and applicable to the new owner-occupant. For the renegotiated lease rent to be so assignable, the new owner-occupant intends to occupy the apartment so long as owning the residential apartment.

Sec. ___-1.11. Renegotiated Lease Rent Exceeding Maximum For New Apartment Owner-Occupant.

When an apartment owner conveys or transfers the leasehold interest in a residential apartment to another person intending to be an owner-occupant and:

(1) The apartment is under lease during a renegotiated rent period; and

(2) The renegotiated lease rent for the apartment is greater than the applicable maximum; the renegotiated lease rent for the apartment shall be reduced by the lessor to the maximum rent chargeable under this chapter and such reduction shall be effective as of the date of occupancy by the new owner-occupant. For the renegotiated lease rent to be so reduced, the new owner-occupant shall execute an affidavit stating that the new owner-occupant intends to occupy the apartment as long as owning the apartment.

Sec.___-1.12. Renegotiated Lease Rent Of Apartment Owner Who Is No Longer Owner-Occupant.

A lessor may reopen the renegotiated lease rent for the residential apartment of an apartment owner who:

(1) Was an owner-occupant of a residential apartment at the time of lease rent renegotiation; but

(2) No longer qualifies as an apartment owner-occupant.

If reopened, the renegotiated lease rent for the residential apartment shall be set in accordance with the lease agreement for persons who are not owner-occupants and shall be effective as of the date of disqualification as provided by this chapter.

Sec.___-1.13. Renegotiated Lease Rent Of New Apartment Owner Who Is Not An Owner-Occupant.

A lessor may reopen the renegotiated lease rent for the residential apartment of an apartment owner when:

(1) The apartment owner has purchased or otherwise received the leasehold interest in a residential apartment from a former owner-occupant; and

(2) The apartment owner does not occupy the residential apartment.

If reopened, the renegotiated lease rent for the residential apartment shall be set in accordance with the lease agreement for persons who are not owner-occupants and shall be effective as of the date of conveyance to the new apartment owner.

Sec.___-1.14. Enforcement.

(a) Any person violating any provision of this chapter shall be subject to a civil fine not exceeding $500.00 for each violation.

(b) The department shall enforce this chapter. Any person may request that the department investigate any alleged violation of any part hereof, or the department on its own initiative may investigate any alleged violation.

(c) Upon receipt of a written request by a person to investigate an alleged violation of this chapter, or upon its own initiative, the department shall conduct an investigation. If finding that a violation has occurred, the department shall attempt an informal correction of the violation. If the violation cannot be informally corrected or if the person requesting the investigation or the alleged violator requests an agency hearing, the department shall:

(1) Hold an agency hearing in accordance with the contested case procedures of chapter 91, Hawaii Revised Statutes; and

(2) Issue an appropriate decision and order. If finding that a violation has occurred, the department may order the violator to do any or all of the following:

(A) Cease and desist from the violation;

(B) Correct the violation;

(C) Pay to a lessor or lessee any amount due and owing as specified in this chapter.

An "amount due and owing" includes excessive lease rent paid by an apartment owner-occupant or insufficient lease rent paid to a lessor; or

(D) Pay the civil fine imposed under subsection (a).

The department may institute a civil action in any court of competent jurisdiction for the enforcement of any decision and order issued pursuant to this section. If finding that a violation has not occurred, whether before or after an agency hearing, the department shall so notify the alleged violator and, if any, the person who requested the investigation. The notification shall be in writing."

SECTION 3. Chapter 13, article 53, Revised Ordinances of Honolulu 1978, as amended, is repealed.

SECTION 4. This ordinance shall take effect upon its approval.

INTRODUCED BY
Andy Mirikitani

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_____
_____
_____
_____

Councilmembers

DATE OF INTRODUCTION:
April 3. 1994
Honolulu, Hawaii

APPROVED AS TO FORM AND LEGALITY:

Deputy Corporation Counsel

APPROVED this ___ day of ___, 1991.

/s/ _____
FRANK F. FASI, Mayor
City and County of Honolulu

_____